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## The American Advantage in Civil Procedure: An Autopsy of the Deutsche Telekom Litigation

Michael Halberstam

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## Article

### The American Advantage in Civil Procedure? An Autopsy of the Deutsche Telekom Litigation

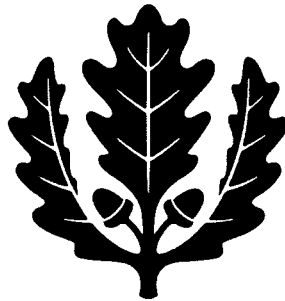
MICHAEL HALBERSTAM

*This Article examines the influence of civil procedure on the legal framework that supports securities markets in the United States and in Germany. It does so by way of comparing parallel shareholder actions against Deutsche Telekom for securities disclosure violations arising out of the same facts and allegations—the first set of actions filed in federal district court in Manhattan, the second filed in district court in Frankfurt, Germany. Deutsche Telekom was accused in both actions of misrepresenting the value of its real estate holdings in its financial disclosures and for failing to disclose negotiations for the acquisition of the U.S. company VoiceStream in its July 2000 offering.*

*But the cases proceeded very differently and produced dramatically different outcomes. Within five years, and after full discovery, the U.S. class action plaintiffs negotiated a \$120 million settlement with the Deutsche Telekom defendants. Meanwhile, the parallel claims by German shareholders, the first of which were filed in 2001, were ultimately dismissed by the German courts in 2012, despite Germany's 2004 adoption of a new and unprecedented aggregate litigation mechanism (dubbed "the Deutsche Telekom law") to afford thousands of complaining German shareholders a reasonable mechanism for pursuing a just and speedier resolution of their claims. Finally, in 2014, the German Supreme Court (Bundesgerichtshof) ruled in favor of plaintiffs on a separate claim, but, to date, German shareholders still have not received any monetary damages. Building on prior research (with Érica Gorga) about the importance of litigation discovery for U.S. corporate and securities laws, this Article examines how German civil procedure gets in the way of private enforcement.*

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# The American Advantage in Civil Procedure? An Autopsy of the Deutsche Telekom Litigation

MICHAEL HALBERSTAM\*

## I. INTRODUCTION

This Article examines the influence of civil procedure on the legal framework that supports securities markets in the United States and Germany—two very different legal systems. It does so by way of comparing parallel shareholder actions against Deutsche Telekom for securities disclosure violations arising out of the same facts and allegations—the first set of actions filed in the U.S. District Court for the Southern District of New York,<sup>1</sup> the second set of actions filed in district court in Frankfurt, Germany.<sup>2</sup>

Deutsche Telekom was accused in both the U.S. and German actions of misrepresenting the value of its real estate holdings in its financial disclosures and for failing to disclose negotiations for the acquisition of the U.S. company VoiceStream in its June 2000 global offering.<sup>3</sup> DT's stock price declined substantially after news of the fifty billion Euro VoiceStream acquisition hit the markets, and again, in February of 2001, after the company took a two billion Euro write-down for a decline in its real estate assets.<sup>4</sup> Shareholders in the United States and in Germany filed suit, claiming that the company had violated its securities disclosure obligations.<sup>5</sup>

But the cases proceeded very differently and produced dramatically different outcomes. U.S. class action plaintiffs filed suit in the Southern

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<sup>1</sup> Consolidated Amended Class Action Complaint, *In re Deutsche Telekom AG Sec. Litig.*, 229 F. Supp. 2d 277 (S.D.N.Y. 2002) (No. 00-CV-9475).

<sup>2</sup> Oberlandesgericht Frankfurt a.M. [OLG Frankfurt] [Higher Regional Court Frankfurt] May 16, 2012, 23 Kap 1/06, *Neue Zeitschrift für Gesellschaftsrecht* [NZG] 747, 2012.

<sup>3</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶¶ 2, 26, 29, 31, 33, 35–36, 42, 44.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

District of New York in December of 2000.<sup>6</sup> After full discovery, plaintiffs negotiated a \$120 million settlement with the Deutsche Telekom defendants.<sup>7</sup> The settlement was approved by the court in June of 2005.<sup>8</sup> Meanwhile, the parallel claims by German shareholders, the first of which were filed in 2001,<sup>9</sup> were ultimately dismissed by the German courts in 2012,<sup>10</sup> despite Germany's late-2004 adoption of a new and unprecedented aggregate litigation mechanism (dubbed "the Deutsche Telekom law") to afford thousands of complaining German shareholders a reasonable mechanism for pursuing a just and speedier resolution of their claims.<sup>11</sup> The case was appealed to the Federal Supreme Court (*Bundesgerichtshof*), which published its decision on October 12, 2014, affirming the Higher Regional Court's judgment on the VoiceStream and real estate allegations, but finding fault with the by now fourteen-year-old lawsuit on grounds that the prospectus illegally classified certain transactions with a subsidiary involving Sprint shares as sales<sup>12</sup>—an issue that was neither complained of nor litigated in New York. As of the publication date of this Article, German shareholders have not received any monetary damages, due to further proceedings in the Frankfurt District Court.

The different developments of these parallel actions speak to the debate about the private enforcement of capital markets regulation in the United States and Europe.<sup>13</sup>

<sup>6</sup> *Id.*

<sup>7</sup> *In re Deutsche Telekom AG Sec. Litig.*, No. 00-CV-9475 (NRB), 2005 U.S. Dist. LEXIS 45798, at \*13 (S.D.N.Y. June 9, 2005).

<sup>8</sup> *Id.* at \*1.

<sup>9</sup> Andreas W. Tilp & Thomas A. Roth, *The German Capital Market Model Proceedings Act as Illustrated by the Example of the Frankfurt Deutsche Telekom Claims*, in MASS TORTS IN EUROPE 131, 134 (Willem H. van Boom & Gerhard Wagner eds., 2014).

<sup>10</sup> Oberlandesgericht Frankfurt a.M. [OLG Frankfurt] [Higher Regional Court Frankfurt] May 16, 2012, 23 Kap 1/06, *Neue Zeitschrift für Gesellschaftsrecht* [NZG] 747, 2012.

<sup>11</sup> See Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act] Aug. 16, 2005, BGBI I at 243, *translation at* [http://www.gesetze-im-internet.de/englisch\\_kapmug/index.html](http://www.gesetze-im-internet.de/englisch_kapmug/index.html) [<https://perma.cc/7BYT-HY6G>]. See generally KÖLNER KOMMENTAR ZUM KAPMUG (Burkhard Hess et al. eds., 2d ed. 2014) [hereinafter KÖLNER KOMMENTAR] (providing law text and academic commentary).

<sup>12</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=pm&Datum=2014&Sort=3&nr=69675&linked=bes&Blank=1&file=dokument.pdf> [<https://perma.cc/QS4G-ZZNA>].

<sup>13</sup> For the U.S. debate, see, for example, Brief of Amici Curiae State of Oregon et al. at 5, *Halliburton Co. v. Erica P. John Fund*, 134 S. Ct. 2398 (2014) (No. 13-217), 2014 WL 526438, at \*5 (arguing to preserve "fraud on the market" doctrine in light of the importance of private enforcement and citing literature); John C. Coffee, Jr., *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 351 (2010) ("[B]oth legal systems could meet at some intermediate point in the not too distant future."); John C. Coffee, Jr. & Hillary A. Sale, *Redesigning the SEC: Does the Treasury Have a Better Idea?*, 95 VA. L. REV. 707, 708–709 (2009); James D. Cox & Randall S. Thomas, *Mapping the American Shareholder Litigation Experience: A Survey of Empirical Studies of the Enforcement of the U.S. Securities Law*, 6 EUR. COMPANY & FIN. L. REV. 164 (2009); Erica Gorga & Michael Halberstam, *Litigation Discovery and Corporate Governance: The Missing Story About*

U.S. regulations have become the template for securities market regulation in Europe, Latin America, and Asia.<sup>14</sup> Many European

"*The Genius of American Corporate Law*", 63 EMORY L.J. 1383, 1386–89 (2014) (discussing literature); Stephen J. Choi & Adam Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison* (Univ. of Mich. Law & Econ. Research Paper Series, Paper No. 12-022, 2014), <http://ssrn.com/abstract=2109739> [<https://perma.cc/4QNM-8VDY>]. In addition, see generally James J. Park, *Rules, Principles, and the Competition to Enforce the Securities Laws*, 100 CALIF. L. REV. 115, 120 (2012) (arguing in support of decentralized securities enforcement); Steven A. Ramirez, *The Virtues of Private Securities Litigation: An Historic and Macroeconomic Perspective*, 45 LOYOLA U. CHI. L.J. 669, 674 (2014) ("[P]rivate securities litigation operates as a key bulwark for securing investor confidence and thus financial stability."); Amanda M. Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship Between Public and Private Enforcement of Rule 10b-5*, 108 COLUM. L. REV. 1301, 1303–04 (2008); Amanda M. Rose, *The Multienforcer Approach to Securities Fraud Deterrence: A Critical Analysis*, 158 U. PA. L. REV. 2173, 2176 (2010) [hereinafter Rose, *Multienforcer Approach*] (arguing for centralization of the securities enforcement process); Matthew C. Stephenson, *Public Regulation of Private Enforcement: The Case for Expanding the Role of Administrative Agencies*, 91 VA. L. REV. 93, 95 (2005) ("[T]he executive branch should have substantially more control over the existence and scope of private enforcement actions . . ."); Jonathan Karpoff et al., *The Legal Penalties for Financial Misrepresentation* 2–3 (May 1, 2007) (unpublished manuscript), <http://ssrn.com/abstract=933333> [<https://perma.cc/WD9V-8ELA>] (providing empirical study of all 697 enforcement actions initiated by the SEC for financial misrepresentation from 1978 through 2004 and comparing penalties from resulting private class action awards).

For the European debate, see, for example, Paolo Giudici, *Representative Litigation in Italian Capital Markets: Italian Derivative Suits and (if Ever) Securities Class Actions*, 6 EUR. COMPANY & FIN. L. REV. 246, 254 (2009) ("Italian law does not grant any inspection right to shareholders of public companies."). In addition, see generally CHRISTOPHER HODGES, *THE REFORM OF CLASS AND REPRESENTATIVE ACTIONS IN EUROPEAN LEGAL SYSTEMS: A NEW FRAMEWORK FOR COLLECTIVE REDRESS IN EUROPE* 78ff (2008); KÖLNER KOMMENTAR, *supra* note 11, at 39–47 (reviewing literature); PROSPEKT- UND KAPITALMARKTINFORMATIONSHAFTUNG: RECHT UND REFORM IN DER EUROPÄISCHEN UNION, DER SCHWEIZ UND DEN USA (K.J. Hopt & H.C. Voigt eds., 2005); Klaus Rotter, *Der Referentenentwurf des BMJ zum KapMuG—Ein Schritt in die Richtige Richtung!*, 12 VERBRAUCHER UND RECHT 443 (2011).

For the European debate about the introduction of class action mechanisms, see generally THE LAW AND ECONOMICS OF CLASS ACTIONS IN EUROPE (Juergen G. Backhaus et al. eds., 2012); AUF DEM WEG ZU EINER EUROPÄISCHEN SAMMELKLAGE? (Mattias Casper et al. eds., 2009) [hereinafter EUROPÄISCHEN SAMMELKLAGE].

For the comparative debate, see KÖLNER KOMMENTAR, *supra* note 11, at 39–47 (reviewing literature); Guido Ferrarini & Paolo Giudici, *Financial Scandals and the Role of Private Enforcement: The Parmalat Case, in AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US* 159 (John Armour & Joseph A. McCahery eds., 2006); John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229, 230 (2007) (arguing that "higher enforcement intensity gives the U.S. economy a lower cost of capital and higher securities valuations"); Eberhard Feess & Axel Halfmeier, *The German Capital Markets Model Case Act (KapMuG): A European Role Model for Increasing the Efficiency of Capital Markets? Analysis and Suggestions for Reform*, 20 EUR. J. FIN. 361 (2014); Gorga & Halberstam, *supra*, at 1479–92 (comparing enforcement and discovery between the United States, Brazil, and Europe); Howell E. Jackson, *Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications*, 24 YALE J. ON REG. 253 (2007) (arguing that the United States expends substantially more resources on public and private securities enforcement than other nations).

<sup>14</sup> CURTIS J. MILHAUPT & KATHARINA PISTOR, *LAW AND CAPITALISM: WHAT CORPORATE CRISES REVEAL ABOUT LEGAL SYSTEMS AND ECONOMIC DEVELOPMENT AROUND THE WORLD* 17–20 (2008); MATTIAS SIEMS, *CONVERGENCE IN SHAREHOLDER LAW* 126 (2008) ("US Securities law today has a model effect that justifies talk of not so much approximation of various legal systems as

countries, including Germany, have adopted the U.S. securities disclosure model and established regulatory agencies that include their own public enforcement divisions.<sup>15</sup> But recourse against issuers for securities disclosure violations remains very limited—especially for the kinds of retail investors who were courted by the Deutsche Telekom offerings.<sup>16</sup> Europeans have recognized that the nature of such claims requires some kind of class action or aggregate litigation mechanism.<sup>17</sup> In the consumer protection context, many European countries have consequently implemented litigation mechanisms that aggregate claims or allow for some kind of representative litigation,<sup>18</sup> but the resistance to exporting U.S.-style class actions to Europe is universal.<sup>19</sup>

By way of a case study, this Article examines how and why private enforcement of securities laws in Europe appears to fail, even after investor-friendly substantive and procedural law changes.

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alignment on American standards from the 1933 and 1934 Act, the SEC Rules, and the NYSE manual.”); see also Gorga & Halberstam, *supra* note 13, at 1386–89 (discussing the corporate governance debate).

<sup>15</sup> See, for example, the European Union’s adoption of the Transparency for Listed Companies Directive (“Transparency Directive”), 2004/109/EC, 2004 O.J. (L 390) 38, as amended in Directive 2013/50/EU, 2013 O.J. (L 294) 13, to improve the uniformity of securities disclosure requirements for issuers whose securities are listed on stock exchanges within the European Union. Like other countries, Germany has passed legislation to implement the Transparency Directive. See *Transparenzlinien-Umsetzungsgesetz* [TUG] [Transparency Directive Implementation Act] Jan. 5, 2007, BGBl I at 10.

<sup>16</sup> Feess & Halfmeier, *supra* note 13, at 361 (“Compared with the USA and other countries with collective procedures in capital markets cases, it is notoriously difficult for small investors in most European countries to get damages for losses caused by wrong or omitted capital markets information.”); see also Andreas W. Tilp, *Das Kapitalanleger-Musterverfahrensgesetz: Stresstest fuer den Telekom-Prozess*, in *FESTSCHRIFT FÜR ACHIM KRÄMER ZUM 70 GEBURTSTAGE* 331 (Uwe Blaurock et al. eds., 2009); Timo Holzborn & Martin Eberhard Foelsch, *Schadenersatzpflichten von Aktiengesellschaften und Deren Management bei Anlegerverlusten—Ein Überblick*, 56 *NEUE JURISTISCHE WOCHENSCHRIFT* 932 (2003).

<sup>17</sup> Feess & Halfmeier, *supra* note 13, at 361; Richard A. Nagareda, *Aggregate Litigation Across the Atlantic and the Future of American Exceptionalism*, 62 *VAND. L. REV.* 1, 3 (2009) (finding that European countries have “come to embrace civil procedure reforms to authorize aggregate litigation”). See generally Samuel Issacharoff & Geoffrey P. Miller, *Will Aggregate Litigation Come to Europe?*, 62 *VAND. L. REV.* 179 (2009) (discussing the repercussions of deregulation across Europe); Gerhard Wagner, *Collective Redress—Categories of Loss and Legislative Options*, 127 *LAW Q. REV.* 55 (2011).

<sup>18</sup> HODGES, *supra* note 13, at 9–13.

<sup>19</sup> HODGES, *supra* note 13, at 131 (“There is a widely quoted mantra in European policy documents that collective mechanisms within the litigation system in the United States operate badly, produce unacceptable results and should not be emulated in Europe.”); see also Nagareda, *supra* note 17, at 6; André Janssen, *Auf dem Weg zu Einer Europäischen Sammelklage?*, in *EUROPÄISCHEN SAMMELKLAGE*, *supra* note 13, at 3, 4–5. See generally Samuel Issacharoff, *Class Actions and State Discovery*, 44 *LOY. U. CHI. L.J.* 369 (2013) (examining the assumptions about state authority that underly U.S.-style class actions).

According to Plaintiffs' attorneys, one major factor in the Deutsche Telekom case was the lack of discovery.<sup>20</sup> In German civil actions, plaintiffs have a very hard time investigating company internal wrongdoing, because of fundamental principles of civil law adjudication that are deeply embedded in German civil procedure.<sup>21</sup> Party-on-party discovery is prohibited.<sup>22</sup> There are no interrogatories,<sup>23</sup> no pretrial witness depositions,<sup>24</sup> and no document discovery.<sup>25</sup> For the most part, parties must obtain documentary evidence in support of their claims independently and extrajudicially.<sup>26</sup> Defendants are not required, and cannot be forced, to produce relevant documents or electronic discovery to support a plaintiff's case.<sup>27</sup> Based on these principles, as well as other principles of due process, the German court (and the U.S. court, acting on principles of comity upon receiving a letter from the German government<sup>28</sup>) refused to allow German plaintiffs in the Deutsche Telekom litigation access to discovery materials that had already been produced in the U.S. litigation.<sup>29</sup> German plaintiffs sought to obtain the documents and deposition transcripts pertinent to their case<sup>30</sup> in U.S. proceedings under 28 U.S.C. § 1782,<sup>31</sup> and the German government went so far as to vehemently object to such disclosure.<sup>32</sup>

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<sup>20</sup> *Bad Connection: A Class Action of Sorts for Germany's Disillusioned Shareholders*, ECONOMIST (Apr. 10, 2008), <http://www.economist.com/node/11021139> [<https://perma.cc/SZA8-GER5>] [hereinafter *Bad Connection*].

<sup>21</sup> See Gorga & Halberstam, *supra* note 13, at 1483–85, 1488–90.

<sup>22</sup> See PETER L. MURRAY & ROLF STÜRNER, GERMAN CIVIL JUSTICE 595 (2004) (“There is no discovery as such.”).

<sup>23</sup> See Kurt Riechenberg, *The Recognition of Foreign Privileges in United States Discovery Proceedings*, 9 NW. J. INT’L L. & BUS. 80, 88 (1988) (“[U]nder the German Code of Civil Procedure, (which has no counterpart to United States pre-trial discovery), parties are not under an unqualified obligation to answer interrogatories . . .”).

<sup>24</sup> See MURRAY & STÜRNER, *supra* note 22, at 241 (“In Germany, there is ordinarily no oral examination of witnesses during the preparatory phases of the proceeding; if a witness is examined, it is always the judge who conducts the questioning.”).

<sup>25</sup> See CIVIL LITIGATION IN COMPARATIVE CONTEXT 223 (Oscar G. Chase et al. eds., 2007) (noting that even though the 2001 reform of Germany’s code of civil procedure introduced a new procedural right to documentary disclosure, procedural orders are not directly enforceable). “While parties and their lawyers can and do conduct their own fact investigations during the case preparation phase, the lack of discovery tools . . . discourage[s] such activities.” MURRAY & STÜRNER, *supra* note 22, at 595 (“There is no discovery as such.”); see also CIVIL LITIGATION IN COMPARATIVE CONTEXT, *supra*, at 207–40 (comparing the discovery mechanisms in England, the United States, Germany, and Japan).

<sup>26</sup> CIVIL LITIGATION IN COMPARATIVE CONTEXT, *supra* note 25, at 223 (“Since the parties do not have a general procedural right to obtain the relevant information, they have to rely on their personal knowledge and on the material in their possession.”).

<sup>27</sup> The basic privilege of a party not to disclose evidence against its own interest, or to open itself up to searching discovery, remains in place in Germany. R.R. VERKERK, FACT-FINDING IN CIVIL LITIGATION: A COMPARATIVE PERSPECTIVE 16 (2010).

<sup>28</sup> *Schmitz v. Bernstein Liebhard & Lifshitz, LLP*, 376 F.3d 79, 81–82, 85 (2d Cir. 2004).

<sup>29</sup> *Id.* at 82.

<sup>30</sup> *Id.* at 81.



This Article thus considers claims about the importance of litigation discovery for corporate and securities laws advanced in previous research (with Érica Gorga) about the importance of litigation discovery for U.S. corporate and securities laws in an article entitled *Litigation Discovery and Corporate Governance: The Missing Story About “The Genius of American Corporate Law”*.<sup>33</sup> There we argued that modern litigation discovery has had a profound impact on the evolution of shareholder litigation, corporate governance, and the culture of corporate disclosure in the United States. We showed how litigation discovery in the United States has driven and structured the process of corporate shareholder litigation;<sup>34</sup> persistently generated information that stimulated the development of case law defining shareholder rights and fiduciary duties;<sup>35</sup> induced incremental improvements in corporate governance practices, including more exacting decision procedures, internal monitoring, record-keeping, and disclosure;<sup>36</sup> established templates for independent corporate internal investigations by boards and regulators;<sup>37</sup> and given regulators steady insight into changing corporate internal practices and patterns of wrongdoing.<sup>38</sup>

This Article explores the corollary to these claims. Does the lack of adequate tools for fact investigation in private litigation in Europe (and other civil law jurisdictions) compromise the enforcement of shareholder rights—even in sophisticated jurisdictions like Germany, which Professor John Langbein famously advocated as a model of efficient fact-finding in his controversial article, *The German Advantage in Civil Procedure*?<sup>39</sup> If so, the German (and European) procedural law would appear unable to support the kind of issuer transparency that European lawmakers have been pursuing.<sup>40</sup>

This Article pursues these comparative questions at a very concrete level, by way of comparing two parallel cases.

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<sup>31</sup> This section of the U.S. Code allows a district court to order a person to produce a document or other thing for use in a foreign proceeding or international tribunal. 28 U.S.C. § 1782(a) (2012).

<sup>32</sup> *Schmitz*, 376 F.3d at 84 (“The German authorities expressed concerns that granting discovery would . . . ‘jeopardize German sovereign rights.’”).

<sup>33</sup> Gorga & Halberstam, *supra* note 13.

<sup>34</sup> *Id.* at 1420–25.

<sup>35</sup> *Id.* at 1455–61.

<sup>36</sup> *Id.* at 1453–54.

<sup>37</sup> *Id.* at 1444–53.

<sup>38</sup> *Id.* at 1479.

<sup>39</sup> John H. Langbein, *The German Advantage in Civil Procedure*, 52 U. CHI. L. REV. 823, 824 (1985).

<sup>40</sup> See, e.g., Dirk A. Verse, *Liability for Incorrect Capital Market Information*, in GERMAN NATIONAL REPORTS ON THE 19TH INTERNATIONAL CONGRESS OF COMPARATIVE LAW 415, 416 (Martin Schmidt-Kessel ed., 2014) (discussing the European Transparency Directive). See generally HEINZ-DIETER ASSMANN & ROLF A. SCHÜTZE, HANDBUCH DES KAPITALANLAGERECHTS (3d rev. ed. 2007).

Part II of this Article describes how concerns about discovery abuse shape the debate about the private enforcement of securities laws in the United States and in Europe. It suggests that European civil law systems, like Germany, cannot promote private enforcement without affording plaintiffs more robust tools of fact investigation. And it explains how the Deutsche Telekom case speaks directly to this debate.

Part III begins by explaining the special significance of the Deutsche Telekom case for the development of the German securities markets. It describes the events that led plaintiffs in both the United States and Germany to file suit and details the factual allegations and legal claims in the U.S. and German complaints.

Part IV compares the development of the litigation in the United States and in Germany. It describes the dramatically different progress of the German and the U.S. cases, the German plaintiffs' attempt to obtain discovery from the United States, the collapse of the German court system in light of the large number of claims, and how a new aggregate litigation mechanism passed by the German parliament in response to this situation shaped the further development of the litigation.

Part V considers the differences in substantive laws and legal standards applied in the United States and in Germany and how they might have influenced the outcome of the litigation.

Part VI examines what inferences we can make about the relative effectiveness of U.S. and German civil procedure from what we have learned. It considers whether the KapMuG statute makes aggregate securities litigation more efficient, whether it gives plaintiffs a fair chance at building their case, and how the comparison reflects back on criticisms of securities class actions in the United States. In so doing, it also acknowledges the difficulties of coming to conclusions about the operation and effects of different civil procedure mechanisms, especially during a time when those mechanisms are undergoing significant changes.

Part VII concludes.

## II. PUBLIC VERSUS PRIVATE ENFORCEMENT: WHOSE ADVANTAGE?

On both sides of the Atlantic, there has been an ongoing debate about the proper relationship between the public and private enforcement of securities laws.<sup>41</sup>

In the United States, the debate has largely been about how much to rein in securities class actions without undermining their deterrent function.<sup>42</sup> Congress and the Supreme Court have repeatedly acted to

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<sup>41</sup> See sources cited *supra* note 13.

<sup>42</sup> See *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007) ("[The Supreme Court] has long recognized that meritorious private actions to enforce federal antifraud securities laws

curtail securities class actions over the past decades, while encouraging greater reliance on public enforcement<sup>43</sup>—especially in the wake of the 2002 Enron and WorldCom scandals.<sup>44</sup> And several scholars who have questioned the current mix of public and private enforcement go so far as to suggest that an exclusive public enforcement model should be considered.<sup>45</sup>

In contrast, the European debate has been about how far to go in private enforcement mechanisms—like aggregate or representative suits—to achieve a speedier resolution of investor claims without opening the door to U.S.-style class actions.<sup>46</sup> Currently, the civil procedure of many E.U. member states is developing mechanisms of aggregate litigation.<sup>47</sup> Policymakers at the E.U. level and in member states recognize that relatively small injuries distributed across a large number of individuals—like consumer product defects, antitrust violations, and securities disclosure violations—cannot be adequately addressed by the courts without special litigation procedures.<sup>48</sup> As we shall see, *Deutsche Telekom* stands for this proposition in German jurisprudence. At the E.U. level, this recognition is reflected in the E.U. “Transparency Directives” for

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are an essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission (SEC). Private securities fraud actions, however, if not adequately contained, can be employed abusively to impose substantial costs on companies and individuals whose conduct conforms to the law.” (citations omitted)). See generally Laura A. McDonald, *Restoring the Balance After the Private Securities Litigation Reform Act of 1995*, 38 FLA. ST. U. L. REV. 911 (2011) (reviewing the debate and relevant policy changes since the 1970s).

<sup>43</sup> See generally Carl W. Hittinger & Jarod M. Bona, *The Diminishing Role of the Private Attorney General in Antitrust and Securities Class Action Cases Aided by the Supreme Court*, 4 J. BUS. & TECH. L. 167 (2009) (discussing *Stoneridge Investment Partners v. Scientific-Atlanta, Inc.*, where the Supreme Court followed the “recent perceived pattern” in securities and antitrust cases to restrict private enforcement mechanisms like class action lawsuits).

<sup>44</sup> DONNA M. NAGY ET AL., *SECURITIES LITIGATION AND ENFORCEMENT: CASES AND MATERIALS* 665 (3d ed. 2012) (noting that the SEC’s congressional appropriations have tripled since 2002, from \$439 million to \$1.2 billion in the fiscal year 2012).

<sup>45</sup> See, e.g., Rose, *Multienforcer Approach*, *supra* note 13, at 2176 (suggesting that the SEC should be granted “exclusive authority to prosecute national securities frauds”).

<sup>46</sup> See *supra* text accompanying notes 14–19 (noting that while Europe, Latin America, and Asia have recognized that the nature of claims against issuers for securities disclosure violations requires some kind of aggregate litigation mechanism, they have resisted the U.S.-style class action, although many have still implemented aggregate litigation mechanisms in the consumer protection context); see also KÖLNER KOMMENTAR, *supra* note 11, at 20, 56 (discussing the need for collective redress mechanisms).

<sup>47</sup> See, e.g., Nagareda, *supra* note 17, at 20–25 (cataloguing the development of aggregate litigation mechanisms in Europe). See generally HODGES, *supra* note 13 (examining mechanisms for collective redress in Europe).

<sup>48</sup> See, e.g., HODGES, *supra* note 13, at 1 (noting that collective redress mechanisms are a “hot topic” in Europe); KÖLNER KOMMENTAR, *supra* note 11, at 1 (defining the scope of Germany’s KapMuG legislation); Roswitha Müller-Piepenkötter, *Geleitwort*, in *EUROPÄISCHEN SAMMELKLAGE*, *supra* note 13, at XI (citing developments at the E.U. level).

improving and establishing uniform standards for public company disclosure.<sup>49</sup> The Transparency Directive, *inter alia*, calls for the member states to adopt aggregate litigation mechanisms, but its legislative history explicitly disclaims the U.S. class action model.<sup>50</sup>

Even as some European countries, like Germany, have passed legislation to do so, public enforcement remains the near exclusive venue for punishing and deterring issuer misconduct.<sup>51</sup> In these debates, the costs of U.S.-style class actions, and in particular of litigation discovery, loom large.<sup>52</sup>

The ability of U.S. plaintiffs to impose substantial discovery costs and burdens on corporate defendants is often viewed as a critical component of successfully prosecuting securities class actions.<sup>53</sup> At the same time, the U.S. retreat from the “private attorney general” model in securities litigation is closely linked with the controversial theory that so-called “impositional discovery” enables plaintiff-side attorneys to pressure defendants to settle based on the threat of discovery rather than the merits of the case.<sup>54</sup> Apart from encouraging meritless (and therefore unjust) strike suits, the critics of securities class actions maintain that the costs and burdens of discovery generate over-deterrence.<sup>55</sup> Limiting plaintiffs’ ability to obtain discovery has thus been the principal point of leverage for U.S. reforms.<sup>56</sup>

Even as Europeans introduce aggregate litigation mechanisms into their domestic law, their reactions to litigation discovery in the U.S. class action setting are extreme. Discovery’s purported excesses are viewed with nothing short of horror—the equivalent of “boiling the ocean to heat a tea

<sup>49</sup> See Directive 2004/109/EC, 2004 O.J. (L 390) 38, *amended by* Directive 2013/50/EU, 2013 O.J. (L 294) 13.

<sup>50</sup> André Janssen, *Auf dem Weg zu Einer Europäischen Sammelklage?*, in EUROPÄISCHEN SAMMELKLAGE, *supra* note 13, at 3, 3.

<sup>51</sup> *Id.*

<sup>52</sup> *Id.* at 4.

<sup>53</sup> See, e.g., Gorga & Halberstam, *supra* note 13, at 1476 & n.490; *Bad Connection*, *supra* note 20 (stating that given the lack of adequate discovery in European securities actions, “we are at a great disadvantage” as compared with the U.S.).

<sup>54</sup> See, e.g., *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007); Michael J. Kaufman & John M. Wunderlich, *The Judicial Access Barriers to Remedies for Securities Fraud*, 75 LAW & CONTEMP. PROBS. 55, 75–76 (2012) (discussing the thesis that plaintiffs can force defendants to settle because of the costs of discovery rather than the strength of the merits of their case); JOHN H. BEISNER, U.S. CHAMBER INST. FOR LEGAL REFORM, *THE CENTRE CANNOT HOLD: THE NEED FOR EFFECTIVE REFORM OF THE U.S. CIVIL DISCOVERY PROCESS* 1–2 (2010), [http://www.instituteforlegalreform.com/uploads/sites/1/ilr\\_discovery\\_2010\\_0.pdf](http://www.instituteforlegalreform.com/uploads/sites/1/ilr_discovery_2010_0.pdf) [<https://perma.cc/567J-FUYQ>] (aggressively promoting discovery reform on behalf of the U.S. Chamber of Commerce).

<sup>55</sup> Kaufman & Wunderlich, *supra* note 54, at 76.

<sup>56</sup> Stephen J. Choi & Robert B. Thompson, *Securities Litigation and Its Lawyers: Changes During the First Decade After the PSLRA*, 106 COLUM. L. REV. 1489, 1492, 1529 (2006); McDonald, *supra* note 42, at 911–12.

kettle” in the words of one observer.<sup>57</sup> Following Langbein, U.S. litigation discovery is considered to be an extremely inefficient way to acquire evidence for the resolution of civil disputes.<sup>58</sup> The rise of electronic discovery has only heightened the sense that Americans are “nuts” when it comes to the scope and tools of litigation discovery, and the resources that are allocated to discovery.<sup>59</sup>

The costs and burdens of litigation discovery are thus at the heart of the debate about how to find the right balance between public and private enforcement in the United States and in Europe. As already mentioned, this debate is longstanding.

In his 1983 article, Langbein championed the efficiency of German civil procedure. He argued that the German civil law process of evidence acquisition and fact-finding by a judge is far superior to the long and wasteful U.S. process of litigation discovery.<sup>60</sup>

In civil law systems, like Germany, judges have a much more active role in civil litigation than U.S. trial court judges do.<sup>61</sup> There is no jury.<sup>62</sup> The judge is the one who resolves all issues of law and fact.<sup>63</sup> The judge identifies the issues, investigates the facts, hears all the evidence, and proceeds issue by issue looking for the fastest way to resolve the dispute.<sup>64</sup> The system is “inquisitorial” in the sense that the judge is always active and drives the proceedings.<sup>65</sup> Proceedings are “episodic” in that there is no single trial.<sup>66</sup>

According to Langbein this inquisitorial approach is far superior, because the judge is able to focus the fact investigation based on the legal issues as they come up.<sup>67</sup> And at each stage of the proceedings only evidence relevant to the particular issue at hand is considered.<sup>68</sup> New evidence may be introduced at any time, which avoids the need to engage

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<sup>57</sup> Interview with Klaus Rotter, named partner of Rotter Rechtsanwälte, in Munich, Ger. (Oct. 7, 2014).

<sup>58</sup> Langbein, *supra* note 39, at 823–24.

<sup>59</sup> See Stephen N. Subrin, *Discovery in Global Perspective: Are We Nuts?*, 52 DEPAUL L. REV. 299, 311–12 (2002).

<sup>60</sup> Langbein, *supra* note 39, at 824.

<sup>61</sup> See MURRAY & STÜRNER, *supra* note 22, at 11.

<sup>62</sup> Langbein, *supra* note 39, at 848.

<sup>63</sup> MURRAY & STÜRNER, *supra* note 22, at 11.

<sup>64</sup> Langbein, *supra* note 39, at 830 (“In German procedure the court ranges over the entire case, constantly looking for the jugular—for the issue of law or fact that might dispose of the case.”).

<sup>65</sup> See *id.* However, while judges drive fact-gathering, Germany’s civil procedure is far from non-adversarial. See *id.* at 841 (“Outside the realm of fact-gathering, German civil procedure is about as adversarial as our own.”).

<sup>66</sup> See *id.* at 830; cf. MURRAY & STÜRNER, *supra* note 22, at 14 (characterizing German civil proceedings as “continuous”). But there is an increasing tendency to consolidate hearings. *Id.*

<sup>67</sup> Langbein, *supra* note 39, at 830.

<sup>68</sup> *Id.*

in useless fact investigation.<sup>69</sup> Much of the work is done via written submissions by the parties.<sup>70</sup> The written depositions recount and interpret the facts for the judge prior to the hearing. The judge will have reviewed the written submissions prior to the hearing and thus is able to focus discussion on questions left unanswered by the submissions.<sup>71</sup>

Langbein argued that U.S. discovery has turned into an adversarial process in which the parties seek to impose unnecessary costs on one another, but also withhold evidence and make accurate fact-finding less likely.<sup>72</sup> He cited excessive preparation of witnesses for depositions as a prime example of the manipulation of evidence in the U.S. adversarial system of party-on-party discovery.<sup>73</sup> In contrast, he argued that there is no such interference with witness testimony in the inquisitorial system.<sup>74</sup> In Germany, the judge interviews the witness directly and can focus the interview on the issues at stake in the lawsuit, always looking to clarify unanswered questions.<sup>75</sup>

Langbein further pointed out that litigators in the United States, who are in control of discovery, have no incentive to limit time spent on discovery, because their compensation is based on hourly fees.<sup>76</sup> In contrast, the German judge is focused on disposing of the case as expediently as possible, because he has a full docket of other cases that require his attention.<sup>77</sup>

Langbein concludes that German procedure is much less costly and much more efficient than the U.S. system.<sup>78</sup>

Langbein's article was highly controversial.<sup>79</sup> And his interpretation of German civil litigation law and practice has been challenged on a number of important points.<sup>80</sup> Critics of Langbein have, for example, pointed out that he limits his comparison to the "traditional bipolar lawsuit in contract, tort, or entitlement" and explicitly excludes from the analysis the "Big Case."<sup>81</sup> But empirical evidence shows that it is in the big cases that

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<sup>69</sup> *Id.* at 831.

<sup>70</sup> *Id.* at 829.

<sup>71</sup> *See id.* at 827–28 (stating that because the judge largely controls the direction of the trial, the judge can focus on issues of particular relevance and importance that have not been resolved).

<sup>72</sup> *Id.* at 841.

<sup>73</sup> *Id.* at 833.

<sup>74</sup> *Id.* at 834.

<sup>75</sup> MURRAY & STÜRNER, *supra* note 22, at 14–15.

<sup>76</sup> *See* Langbein, *supra* note 39, at 829.

<sup>77</sup> *See id.* at 827.

<sup>78</sup> *Id.* at 866.

<sup>79</sup> *See* Ronald J. Allen et al., *The German Advantage in Civil Procedure: A Plea for More Details and Fewer Generalities in Comparative Scholarship*, 82 NW. U. L. REV. 705, 707 (1988).

<sup>80</sup> Michael Bohlander, *The German Advantage Revisited: An Inside View of German Civil Procedure in the Nineties*, 13 TUL. EUR. & CIV. L.F. 25, 28–29 (1998).

<sup>81</sup> *Id.* at 708 (citing Langbein, *supra* note 39, at 825).

discovery generates substantial costs and extended discovery, whereas many small cases are resolved with very limited discovery and a significant percentage with no discovery at all.<sup>82</sup>

It is in the so-called “Big Cases,” where plaintiffs must obtain evidence about wrongdoing by large corporations or government that U.S. litigation discovery becomes a critical tool.<sup>83</sup> In this vein, I have argued in a previous paper (with Érica Gorga) that litigation discovery has had a profound impact on the development of U.S. corporate and securities laws, and, more broadly, on the U.S. culture of corporate transparency.<sup>84</sup> In this article, we describe in detail how litigation discovery shines a bright light on corporate internal events and practices when it is allowed.<sup>85</sup> Depositions, document requests, interrogatories, the attorney subpoena power, and third party discovery subject company internal operations, business practices, decision procedures, and specific events to intense scrutiny by outside gatekeepers and party-opponents.<sup>86</sup> We show how the tools and the reach of litigation discovery have become embedded in U.S. practices of public and private enforcement, in corporate internal governance and practices of communication and information management, in the law of fiduciary duty, and in the expectations of market participants.<sup>87</sup> Contrary to popular views about the unaccountability of corporate directors and officers, we conclude that U.S. corporations are fairly transparent.<sup>88</sup>

But in Europe, there is no litigation discovery.<sup>89</sup> There is no specific phase of the litigation process dedicated to the exploration or collection of evidentiary materials in civil law systems.<sup>90</sup> Nor is there a general right to obtain relevant information in connection with the proceedings.<sup>91</sup> Party-on-party discovery is not permitted and any demand for information from a

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<sup>82</sup> EMERY G. LEE III & THOMAS E. WILLGING, FED. JUDICIAL CTR., PRELIMINARY REPORT TO THE JUDICIAL CONFERENCE ADVISORY COMMITTEE ON CIVIL RULES 35 tbl.4, 38 tbl.6 (2009), [http://www.fjc.gov/public/pdf.nsf/lookup/dissurv1.pdf/\\$file/dissurv1.pdf](http://www.fjc.gov/public/pdf.nsf/lookup/dissurv1.pdf/$file/dissurv1.pdf) [https://perma.cc/X2RQ-9JP9].

<sup>83</sup> See Allen et al., *supra* note 79, at 709 (“In the ‘Big Case,’ enormous time and resources are invested in discovery, preparation and trial . . .”).

<sup>84</sup> Gorga & Halberstam, *supra* note 13, at 1395.

<sup>85</sup> *Id.*

<sup>86</sup> *Id.* at 1398.

<sup>87</sup> *Id.* at 1394.

<sup>88</sup> An exception to the populist belief in corporate secrecy can be found in DON TAPSCOTT & DAVID TICOLL, *THE NAKED CORPORATION: HOW THE AGE OF TRANSPARENCY WILL REVOLUTIONIZE BUSINESS*, at xii (2003). But Tapscott and Ticoll do not consider how the principles and practices of litigation discovery have contributed to this result.

<sup>89</sup> CIVIL LITIGATION IN COMPARATIVE CONTEXT, *supra* note 25, at 222.

<sup>90</sup> *Id.*

<sup>91</sup> See MURRAY & STÜRNER, *supra* note 22, at 277 (explaining that a party must file a request with the judge to obtain inspection of documents and things from an opposing party, but that there is no general right to obtain such information).

defendant must be approved and issued by a judge. The parties are thus expected to rely on their personal knowledge and any materials in their possession to make out their case. While there are some substantive and procedural rights to obtain information under certain circumstances—the main procedural tool is a shifting of the burden of proof—these are limited.<sup>92</sup> A plaintiff must obtain evidence of corporate internal wrongdoing from other sources, like investigative journalism, government investigations, or whistleblowers. Plaintiff-side attorneys thus view companies as “black boxes” which they are able to penetrate only under special circumstances. German plaintiffs, like plaintiffs in other European countries,<sup>93</sup> “practically have no access to . . . [an issuer’s] files”—“[o]nly prosecutors have the weapons to seize papers, question witnesses and find out what actually happened.”<sup>94</sup>

But Langbein’s view of U.S. civil litigation, and especially discovery, appears still to be widely shared, especially in Europe. European policymakers are thus, in a sense, attempting to square the circle. On the one hand, they recognize the importance of aggregate litigation. On the other, they are unwilling to afford plaintiffs the tools that are necessary to investigate large public companies in a private enforcement proceeding. In the words of Professor Richard Nagareda, “Europe consciously seeks to avoid the U.S. experience,” by attempting “to harness the closure potential of aggregation, without its enabling potential.”<sup>95</sup>

The debate about who has the advantage in civil procedure when it comes to shareholder and securities litigation is therefore still very much alive in the contemporary struggle to establish and maintain the legal preconditions to strong securities markets. While the corporate governance debate has in some ways moved on, policymakers are very much occupied with this question at present.

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<sup>92</sup> See MURRAY & STÜRNER, *supra* note 22, at 268 (“[A]locations of burden of proof often flow from the considerations of relative accessibility and practicality of proof . . .”).

<sup>93</sup> “Given the lack of efficient discovery rules, investor action against mass wrongdoings is virtually impossible in Italy as it is in the rest of Europe, unless information is gathered by public authorities.” Ferrarini & Giudici, *supra* note 13, at 201 (citation omitted).

<sup>94</sup> Karin Matussek, *Porsche Plaintiffs Seek \$5 Billion with Limited Tools*, BLOOMBERG BUS. (June 26, 2012), <http://www.bloomberg.com/news/articles/2012-06-25/porsche-plaintiffs-seek-5-billion-with-limited-tools> [<https://perma.cc/TWD7-H88D>] (“Different from the U.S., plaintiffs here have no pre-trial discovery, so they practically have no access to Porsche’s files . . . . Only prosecutors have the weapons to seize papers, question witnesses and find out what actually happened.” (quoting law professor Thomas Moellers)); *Bad Connection*, *supra* note 20 (“‘Compared with America we are at a great disadvantage,’ says Andreas Tilp, whose law firm is spearheading the model trial on behalf of shareholders. . . . Most aggravating for Mr. Tilp is his inability to secure documents, such as a Bonn prosecutor’s report that he believes concludes there was balance-sheet fraud, and another report from the Federal Audit Court, which was pivotal in the American settlement.”). A substantial portion of the Bonn prosecutor’s documents were finally obtained before the 2008 hearings by the plaintiffs.

<sup>95</sup> Nagareda, *supra* note 17, at 9.



## III. BACKGROUND AND COMPLAINTS

A. *Background*

The Deutsche Telekom case is of particular importance for understanding the development of private enforcement of securities laws in Germany. It was the largest German shareholder litigation ever.<sup>96</sup> And it involved share issuances that had a special significance for the German securities markets as a whole.

The company resulted from the German government's decision to privatize its telecommunications monopoly, which was part of the larger government-run Deutsche Bundespost. Deutsche Telekom's 1996 Initial Public Offering, which raised approximately \$20 billion, was not just the largest IPO in Europe ever—it represented a signal initiative to push forward the German government's efforts to liberalize Germany's financial markets and create a German shareholder culture.<sup>97</sup> During the 1990s, German policymakers were rewriting German financial market regulations to encourage greater investment in new technology startups, increase the number of publicly held firms, create a market for firms, and, generally, diversify away from the traditional, highly concentrated, German bank-centered model of corporate finance towards a U.S. model of greater reliance on the stock markets to capitalize firms.<sup>98</sup> In this context, the Deutsche Telekom IPO's success was of great importance.

Deutsche Telekom's IPO took place in 1996, the first secondary offering was placed in 1999, and another offering followed in May/June 2000.<sup>99</sup> The share offerings were advertised as a Volksaktie (the "people's share"),<sup>100</sup> and both the privatization and offerings included unusual features designed to encourage and sustain widespread share ownership.<sup>101</sup> Approximately forty percent of the 1996 share offering was allocated to retail investors.<sup>102</sup> Retail investors could purchase the shares at a discount.<sup>103</sup> And the German government initially held onto seventy-four percent, which could have been interpreted to mean that the government

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<sup>96</sup> Tilp, *supra* note 16, at 332 (citing press reports).

<sup>97</sup> Jeffrey N. Gordon, *Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany: Deutsche Telekom and DaimlerChrysler 2–4* (Columbia Law Sch. Ctr. for Law & Econ. Studies, Working Paper No. 161, 2000), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=208508](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=208508) [<https://perma.cc/464V-BMLG>] ("One of the major recent objectives of German economic policymakers has been the promotion of a shareholding culture among German citizens.").

<sup>98</sup> *Id.* at 2–3.

<sup>99</sup> These offerings are referred to in the litigation as DT1, DT2, and DT3.

<sup>100</sup> Tilp & Roth, *supra* note 9, at 132.

<sup>101</sup> Gordon, *supra* note 97, at 15; Tilp & Roth, *supra* note 9, at 133.

<sup>102</sup> Gordon, *supra* note 97, at 13.

<sup>103</sup> By contrast, the market places a premium on large blocks of shares.

stood behind the company. Deutsche Telekom announced that it expected to pay a two percent dividend in 1997 and a four percent dividend in 1998, which Professor Jeffrey Gordon called “a somewhat remarkable undertaking for a company in the midst of a fundamental business change.”<sup>104</sup> Finally, the public landline telephone monopoly comprised a substantial part of Deutsche Telekom’s business. With a new government regulatory agency setting the rates, “[a] prospective shareholder could well find in these dividend arrangements an implicit promise that the Regulatory Authority will set a rate structure so as to permit payment of a regular dividend regardless of the profitability of Deutsche Telekom’s other business activities.”<sup>105</sup>

The litigation against Deutsche Telekom and its co-defendants in the United States and Germany followed unscheduled disclosures by the company in July of 2000 and in February of 2001.

On July 24, 2000, Deutsche Telekom disclosed that it was acquiring the U.S. cellular and telecommunications company VoiceStream for around fifty billion dollars.<sup>106</sup> The extraordinary price Deutsche Telekom would pay to enter the highly competitive U.S. cellular market raised serious concerns among investors. As a result, the company’s share price dropped by thirteen percent on the day of the VoiceStream announcement.<sup>107</sup> By December of 2000, shares had dropped by thirty percent amid declining profits and a slump of European telecommunication shares.<sup>108</sup>

The disclosure of the VoiceStream acquisition came only four weeks after the company first listed its shares on the New York Stock Exchange (NYSE) on June 19, 2000, but was disclosed neither in the May 22 Registration Statement that it filed with the SEC, nor its June 17 U.S. prospectus for the American Depositary Shares.<sup>109</sup> Likewise, the May 2000 German offering and three supplements, the last of which was published in June of 2000, contained no mention of the VoiceStream acquisition.<sup>110</sup>

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<sup>104</sup> Gordon, *supra* note 97, at 15.

<sup>105</sup> *Id.* In order to reduce its ownership of Deutsche Telekom to below fifty percent, the German government sold a large block of shares to the German Kreditanstalt fuer Wiederaufbau (KfW), the public entity created to serve as a development bank for Eastern Germany after the collapse of the GDR. KfW is the development bank that was created by the German government to help finance economic development in the former East German territories.

<sup>106</sup> Nicole Harris et al., *Deutsche Telekom Agrees to Acquire VoiceStream Wireless for \$50.7 Billion*, WALL ST. J. (July 24, 2000), <http://www.wsj.com/articles/SB964424432543482052> [<https://perma.cc/86D7-Q9MV>].

<sup>107</sup> Vanessa Fuhrmans, *German Firm Faces Suit over Offering—Deutsche Telekom Didn’t Reveal Plans, Lawyers Contend*, WALL ST. J., Dec. 15, 2000, at A13.

<sup>108</sup> *Id.*

<sup>109</sup> *Id.*

<sup>110</sup> See Tilp, *supra* note 16, at 338.

The decision to acquire VoiceStream would cost Deutsche Telekom dearly. In 2002, Deutsche Telekom wrote off around eighteen billion dollars in assets relating to VoiceStream, contributing to a loss of \$24.7 billion for the first nine months of 2002. The timing of the acquisition, at the height of the dot-com bubble, was a major factor in this result.

In February of 2001, Deutsche Telekom issued another unscheduled disclosure. The February disclosure announced the revaluation of Deutsche Telekom's substantial real estate holdings in the amount of more than two billion Euros (or \$1.8 billion).<sup>111</sup> The depreciation of the pretax value of its real estate holdings would cut estimated net income in 2000 by 1.4 billion Euros, revealing a fourth-quarter loss of 2.5 billion Euros.<sup>112</sup>

Deutsche Telekom's share price dropped again. On the Frankfurt stock exchange, Deutsche Telekom's so-called T-Share (T-Aktie) was priced at 14.57 Euros in its initial 1996 European IPO. It reached a record 103 Euros, but then dropped back to around sixty Euros just before the third stock issuance in June 2000.<sup>113</sup>

The valuation of Deutsche Telekom's real estate holdings had, by this time, become the subject of a government investigation by a German prosecutor in Bonn.<sup>114</sup> The investigation, which was initiated on July 24, 2000, the same day on which Deutsche Telekom disclosed the VoiceStream acquisition, followed disclosures in the press that Deutsche Telekom had intentionally applied inappropriate valuation methods, going back all the way to its 1996 public financial statements, and had consequently overstated Deutsche Telekom's assets substantially.<sup>115</sup>

### B. *The U.S. Complaint*

Deutsche Telekom shareholders who bought American Depository Shares in the June 2000 offering filed suit in the U.S. District Court for the Southern District of New York in December of 2000 against the company, certain control persons, and its underwriters. The complaint named as defendants (1) Deutsche Telekom, (2) its Chairman and CEO Ron Sommer, who signed the Registration Statement; (3) the German public

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<sup>111</sup> William Boston, *Deutsche Telekom Cuts Net Estimates on Big Write-Down*, WALL ST. J., Feb. 22, 2001, at A14.

<sup>112</sup> *Id.*

<sup>113</sup> Deutsche Telekom AG, Annual Report for Fiscal Year Ending Dec. 31, 2000 (Form 20-F), at 100 (May 4, 2001).

<sup>114</sup> Deutsche Telekom AG, Annual Report (Form 20-F/A), at 46 (Feb. 26, 2002).

<sup>115</sup> William Boston, *Deutsche Telekom's Stance on Real Estate Is Disputed—Former Executive Alleges Company Knew Figures Were Too High in 1995*, WALL ST. J., Mar. 19, 2001, at A14.

development bank, KfW, which had owned the shares that were sold as ADSs in the U.S. public offering; and (4) the underwriters.<sup>116</sup>

The Amended Class Action Complaint alleged that the May 22, 2000 Registration Statement and subsequent versions of the U.S. Offering were materially false and misleading in that they (1) failed to disclose that Deutsche Telekom was at that time engaged in advanced merger talks with VoiceStream Wireless Corp., and (2) overstated Deutsche Telekom's real estate portfolio by at least two billion Euros.<sup>117</sup>

Plaintiffs brought claims against all of the defendants under Sections 11 and 12(a)(2) of the Securities Act of 1933. The complaint charges Deutsche Telekom's Chief Executive Officer, Ron Sommer, and KfW with "control person liability" under Section 15 and 20 of the Securities Act for Deutsche Telekom's violation of Section 11 and Section 12(a)(2).<sup>118</sup> The complaint also charges Deutsche Telekom, Ron Sommer, and KfW with securities fraud pursuant to Section 10(b) of the Securities Exchange Act, and Rule 10b-5 thereunder.<sup>119</sup>

Section 11 imposes strict liability on issuers for material misstatements or omissions in a registration statement and provides for damages (not to exceed in amount the price at which the securities were originally offered).<sup>120</sup> Directors, underwriters, and non-issuers charged under Section 11 have a "due diligence defense."<sup>121</sup>

Section 12(a)(2) overlaps with Section 11 in that it establishes a private right of action for rescission against anyone who "offers or sells a security" using a materially false or misleading prospectus (or oral communication).<sup>122</sup> "Like Section 11, Section 12(a)(2) waters down the traditional elements of common law fraud."<sup>123</sup> Thus, under Section 12(a)(2), the plaintiff does not have to prove scienter, causation, or reliance. Under 12(a)(2) defendants also have a defense of reasonable care, or may avoid liability based on negative causation.<sup>124</sup>

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<sup>116</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶¶ 9–16. These underwriters included: Deutsche Bank AG, Deutsche Bank Alex. Brown Inc., Dresdner Kleinwort Benson North America, Goldman Sachs & Co., and A.G. Edwards & Sons, Inc.

<sup>117</sup> *Id.* ¶¶ 27–29.

<sup>118</sup> *Id.* ¶¶ 23–24.

<sup>119</sup> *Id.* ¶ 3.

<sup>120</sup> Securities Act of 1933, ch. 38, § 11, 48 Stat. 74, 82 (codified as amended at 15 U.S.C. § 77k (2012)).

<sup>121</sup> *Escott v. Barchriss Constr. Corp.*, 283 F. Supp. 643, 697–98 (S.D.N.Y. 1968).

<sup>122</sup> Securities Act of 1933 § 12(a)(2) (codified as amended at 15 U.S.C. § 77l(a)(2) (2012)).

<sup>123</sup> *NAGY ET AL.*, *supra* note 44, at 308 (citing *Gustafson v. Alloyd Corp.*, 513 U.S. 561, 571, 581 (1995)).

<sup>124</sup> Securities Act of 1933 § 12(b) (codified as amended at 15 U.S.C. § 77l (2012)).

Finally, Section 10(b) of the Securities Exchange Act,<sup>125</sup> and Rule 10b-5 thereunder,<sup>126</sup> are the basis for a private right of action for securities fraud. Under 10b-5, a plaintiff must establish scienter and causation, and is subject to the heightened pleading standards of the Private Securities Litigation Reform Act of 1995, which, *inter alia*, require plaintiffs to plead particularized facts that establish a “strong inference” of scienter in order to overcome a motion to dismiss.<sup>127</sup>

### 1. *VoiceStream Allegations*

Deutsche Telekom filed a registration statement with the SEC on May 22, 2000, as part of a global offering of 200 million shares, 45 million of which were to be sold as American Depositary Receipts (ADRs).<sup>128</sup>

Plaintiffs alleged that by June 16, 2000, the effective date of the Registration Statement, Deutsche Telekom “had already completed advanced merger negotiations with VoiceStream,”<sup>129</sup> agreeing to offer \$200 per share for VoiceStream’s stock and planning to fund the transaction primarily by issuing millions of shares of Deutsche Telekom stock.<sup>130</sup> The prospectus contained a general reference to Deutsche Telekom’s strategy of growth by acquisition, as follows:

Deutsche Telekom and its affiliates are actively considering and discussing a number of potential acquisition transactions. These may be made using newly issued shares or in the aggregate be material to Deutsche Telekom or its affiliates, cash or a combination of cash and shares, and may individually or in the aggregate be material to Deutsche Telekom or its affiliates. Discussions with third parties may be commenced or discontinued at any time.<sup>131</sup>

Plaintiffs alleged this statement was materially false and misleading, and omitted to disclose material facts, because it failed to disclose the advanced negotiations with VoiceStream.<sup>132</sup>

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<sup>125</sup> Securities Exchange Act of 1934, ch. 404, § 10(b), 48 Stat. 881, 891 (codified as amended at 15 U.S.C. § 78j (2012)).

<sup>126</sup> 17 C.F.R. 240.10b-5 (2014).

<sup>127</sup> Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, § 101(b), 109 Stat. 737, 743 (codified as amended at 15 U.S.C. § 78u-4(b)(2)(A) (2012)).

<sup>128</sup> *In re Deutsche Telekom AG Sec. Litig.*, No. 00 CIV 9475 SHS, 2002 WL 244597, at \*2 (S.D.N.Y. Feb. 20, 2002).

<sup>129</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33.

<sup>130</sup> *Id.* ¶ 29.

<sup>131</sup> DEUTSCHE TELEKOM, SUPPLEMENT NO. 3 TO THE SALES PROSPECTUS DATED MAY 26, 2000, at 4 (2000), <http://www.telekom.com/investor-relations/publications/IPO-s-1996-2000/201632> (follow “DT3 in 2000” hyperlink) [hereinafter DT PROSPECTUS SUPPLEMENT].

<sup>132</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 29.

The plaintiffs set forth the timeline of the merger negotiations as follows:

The plaintiffs alleged that Deutsche Telekom contacted John W. Stanton, the chairman and chief executive officer of VoiceStream on March 7, 2000 to inform him Deutsche Telekom was interested in acquiring VoiceStream and to arrange a meeting.<sup>133</sup> They further alleged that Stanton and Ron Sommer met on March 13, 2000 in New York to discuss Deutsche Telekom's interest in acquiring VoiceStream.<sup>134</sup> Later that month, on March 29, 2000, a second meeting occurred at which Deutsche Telekom outlined its proposal for a share exchange.<sup>135</sup> Stanton allegedly rejected the proposal because, *inter alia*, Deutsche Telekom's shares were not publicly traded.<sup>136</sup>

In the meantime, Deutsche Telekom proceeded with its Global Offering and the preparation for its U.S. Registration Statement and public listing of the ADSs on the New York Stock Exchange.<sup>137</sup> On May 22, 2000, Deutsche Telekom filed its Registration Statement with the SEC.<sup>138</sup> Then on June 1, 2000, Deutsche Telekom allegedly contacted VoiceStream again to ask whether VoiceStream would consider an equity investment.<sup>139</sup> VoiceStream responded by saying it would consider a written proposal "if it was submitted no later than early June."<sup>140</sup> Sommer and Stanton further discussed the acquisition by telephone.<sup>141</sup>

Five days later, on June 6, 2000, Deutsche Telekom submitted its written proposal to acquire all of VoiceStream's shares at a price within the range of \$170–\$190 per share.<sup>142</sup> On June 12, 2000, Stanton replied in writing that VoiceStream would not consider an offer for less than \$200 per share, part of which would have to be consideration in cash.<sup>143</sup> VoiceStream also offered to permit Deutsche Telekom to begin limited due diligence if Deutsche Telekom believed it could raise its offer to \$200 per share.<sup>144</sup> On June 15, 2000, Stanton and Sommer discussed the terms of the

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<sup>133</sup> *Id.* ¶ 33(a).

<sup>134</sup> *Id.*

<sup>135</sup> *Id.* ¶ 33(b).

<sup>136</sup> *Id.*

<sup>137</sup> *Id.* ¶ 26.

<sup>138</sup> *In Re Deutsche Telekom AG Sec. Litig.*, No. 00 CIV 9475 SHS, 2002 WL 244597, at \*2 (S.D.N.Y. Feb. 20, 2002); Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 1.

<sup>139</sup> *Deutsche Telekom*, 2002 WL 244597, at \*2; Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33(c).

<sup>140</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33(c).

<sup>141</sup> *Id.*

<sup>142</sup> *Deutsche Telekom*, 2002 WL 244597, at \*2; Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33(d).

<sup>143</sup> Sources cited *supra* note 142.

<sup>144</sup> *Id.*

deal again, according to the plaintiffs.<sup>145</sup> Deutsche Telekom allegedly agreed to offer at least \$200 per share for VoiceStream stock, and VoiceStream began providing Deutsche Telekom with due diligence materials.<sup>146</sup>

On June 16, 2000, Deutsche Telekom's Registration Statement became effective. It included no mention of VoiceStream.<sup>147</sup> The final sales prospectus, which was dated June 17, 2000, again included no mention of VoiceStream.<sup>148</sup>

The share offering was a firm commitment underwriting by which the underwriters agreed to buy 200 million ordinary shares of Deutsche Telekom from KfW as part of a global offering in fifteen European countries and the United States.<sup>149</sup> KfW paid underwriting commissions and fees in the amount of \$1.033 per ADS.<sup>150</sup> The underwriters also had the option and did purchase another 30 million shares from KfW to cover overallotments.<sup>151</sup> The offering price by the underwriters to the public was \$64.38 per share.<sup>152</sup> On June 16, 2000, the effective date of the Registration Statement, the closing price of the ADSs on the NYSE was \$65 per share.<sup>153</sup>

On July 11, 2000, news broke that Deutsche Telekom planned to pay at least \$30 billion to acquire VoiceStream.<sup>154</sup> The share price of Deutsche Telekom dropped on this news.<sup>155</sup> Additional details about the Deutsche Telekom/VoiceStream merger were disclosed in the news from July 12 through July 23, 2000.

Finally, on July 24, 2000, Deutsche Telekom publicly announced its planned \$50.7 billion acquisition of VoiceStream.<sup>156</sup> The disclosure reported VoiceStream shareholders would receive 3.2 shares of Deutsche Telekom and \$30 in cash for each share as consideration for the merger.<sup>157</sup> "Continuing the downward trend of the previous days in reaction to news

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<sup>145</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33(c).

<sup>146</sup> *Id.*

<sup>147</sup> *Deutsche Telekom*, 2002 WL 244597, at \*2.

<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *Id.*

<sup>151</sup> *Id.*

<sup>152</sup> *Id.*

<sup>153</sup> *Id.*

<sup>154</sup> Malcolm Fried, *Deutsche Telekom in U.S. Deal?*, L.A. TIMES (July 11, 2000), <http://articles.latimes.com/2000/jul/11/business/fi-51028> [<https://perma.cc/X3W4-Y3DV>].

<sup>155</sup> *Deutsche Telekom*, 2002 WL 244597, at \*2.

<sup>156</sup> Nicole Harris et al., *Deutsche Telekom, VoiceStream Boards Approve \$50.5 Billion Cash, Stock Bid*, WALL ST. J., July 24, 2000, at A3.

<sup>157</sup> Press Release, VoiceStream Wireless Corp., Deutsche Telekom to Acquire VoiceStream for \$50.7 Billion, Creating First Wireless Operator Using GSM Standard Worldwide (July 24, 2000), <http://www.sec.gov/Archives/edgar/data/946770/000095012300006755/e425.txt> [<https://perma.cc/9Z7R-4UNQ>].

of the merger,” the Complaint states, “shares of [Deutsche Telekom] declined almost seven dollars per share on July 24 to approximately \$45 per share.”<sup>158</sup>

## 2. Real Estate Allegations

The U.S. plaintiffs also challenged Deutsche Telekom’s Registration Statement and Prospectus on grounds that they contained material misstatements and omissions with respect to Deutsche Telekom’s real estate portfolio and related assets.<sup>159</sup> The reported book value of Deutsche Telekom’s real estate assets were 17.2 billion Euros as of December 31, 1999, the final quarter of 1999.<sup>160</sup> Deutsche Telekom’s real estate assets contributed to a total reported 37.709 billion Euros in shareholder equity as of March 31, 2000, with total assets for the company reported at 101.477 billion Euros as of March 31, 2000.<sup>161</sup> Deutsche Telekom had also established certain reserves or recognized charges for each of the past three years to cover “potential losses associated with the disposition of properties no longer used in this business.”<sup>162</sup>

But in February 21, 2001, only seven months after the July 19 offering, Deutsche Telekom announced it was taking a special write-down of two billion Euros (approximately \$1.8 billion) for the land values in its real estate portfolio.<sup>163</sup> Deutsche Telekom’s share price dropped on this announcement.<sup>164</sup> Moreover, on March 19, 2001, Deutsche Telekom’s CFO, Karl-Gerhard Eich, stated “I can’t say at this point whether [the two billion Euro write-down] will be enough.”<sup>165</sup>

The plaintiffs alleged the company’s real estate portfolio had been substantially overvalued at the time of the Offering.<sup>166</sup> Deutsche Telekom had valued its real estate assets by grouping them into types of properties and then estimating their current market value.<sup>167</sup> The company claimed this so-called “cluster method” of valuing its real estate assets represented the best approximation of their value because the properties were too

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<sup>158</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 32.

<sup>159</sup> *Id.* ¶ 34.

<sup>160</sup> DT PROSPECTUS SUPPLEMENT, *supra* note 131, at 47.

<sup>161</sup> *Id.* at 9.

<sup>162</sup> *Id.* at 127.

<sup>163</sup> *Deutsche Telekom Will Incur Charge for Real-Estate Holdings*, DOW JONES BUS. NEWS, Feb. 21, 2001, Factiva.

<sup>164</sup> *Stock Markets Across the Globe Finish Lower as U.S. Technology Stocks Slide*, DOW JONES BUS. NEWS, Feb. 21, 2001, Factiva.

<sup>165</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 43.

<sup>166</sup> *Id.* ¶ 44.

<sup>167</sup> Boston, *supra* note 115.



numerous to value individually, and historical records for the properties were unavailable.<sup>168</sup>

The February 2001 write-down followed longstanding questions about the cluster method. Friedrich Goerts, the former chief of Deutsche Telekom's real estate unit, had blown the whistle on what he perceived to be "vastly overvalued" real estate assets as early as 1995.<sup>169</sup> Goerts and others claimed the true market value (or fair value) of Deutsche Telekom's real estate assets were much lower.<sup>170</sup> Whenever the company sold property it would have to take a write-down for realized losses.<sup>171</sup> But the company's December 1998 and 1999 financial statements, as well as the March 31, 2000 summary financial information for the quarter—all of which were included in the U.S. Registration Statement—reported Deutsche Telekom's real estate assets on the basis of the cluster method.<sup>172</sup> In September 1998, Goerts finally wrote a letter to senior executives stating he could no longer participate in what he considered to be balance sheet fraud.<sup>173</sup> Goerts was subsequently fired.<sup>174</sup> Statements by Goerts accusing Deutsche Telekom of balance sheet fraud were first published in the German news magazine *Der Spiegel* on February 12, 2001, and subsequently in a March 19, 2001 *Wall Street Journal* article covering the write-down.<sup>175</sup>

Plaintiffs charged that the U.S. Registration Statement was false and misleading because it misreported the fair value of the real estate holdings and failed to reconcile those numbers with U.S. Generally Accepted Accounting Principles as required by SEC rules.<sup>176</sup>

Because Deutsche Telekom and its CEO Ron Sommer had knowledge of the alleged overvaluation, plaintiffs charged them with securities fraud under Rule 10b-5.<sup>177</sup>

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<sup>168</sup> Oberlandesgericht Frankfurt a.M. [OLG Frankfurt] [Higher Regional Court Frankfurt] July 3, 2013, *Neue Zeitschrift für Gesellschaftsrecht* [NZG] 1103, 2013 ("Dies erfolgte nicht in Form einer Bewertung jeder einzelnen Immobilie, vielmehr wurde nur ein Teil derselben (z.B. in Großstadtlagen und solche, die ab 1993 erworben worden waren) individuell bewertet, während die anderen in verschiedene Gruppen (Cluster) aufgeteilt und nach durchschnittlichen Werten für diese Cluster bewertet wurden.").

<sup>169</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 44(a).

<sup>170</sup> Boston, *supra* note 115.

<sup>171</sup> *Id.*

<sup>172</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶¶ 49–50; DT PROSPECTUS SUPPLEMENT, *supra* note 131, at 46–47, 126–27, F-45 to F-46.

<sup>173</sup> Boston, *supra* note 115.

<sup>174</sup> *Id.*

<sup>175</sup> See *id.* (describing Goerts's fears that he was being made a scapegoat for the real estate valuations).

<sup>176</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶¶ 49–52, 54–55.

<sup>177</sup> *Id.* ¶¶ 89–90.

### C. The German Complaint<sup>178</sup>

The complaints filed against Deutsche Telekom in Frankfurt, Germany, contained many additional allegations and claims against the company, but included the two central claims that Deutsche Telekom was liable for damages or rescission for its failure to disclose the advanced merger negotiations with VoiceStream, and for falsely valuing its real estate assets in its German May 2000 offering.<sup>179</sup> The liability claims were actionable under Sections 44 and 45 of the German Securities Exchange Act (*BörsenGesetz*).<sup>180</sup> The real estate allegations also sounded in fraud, with plaintiffs invoking certain tort and criminal law claims and remedies.<sup>181</sup>

Section 44 of the *BoersG* provides investors who have purchased securities based on a false or incomplete statement the right to sue issuers and other “responsible parties” for rescission or damages not to exceed the purchase price of the securities.<sup>182</sup> Section 45(1) provides for an affirmative defense for defendants who can show that they had no knowledge of the mistake or omission and that their lack of knowledge did not result from gross negligence.<sup>183</sup>

The German substantive law thus differed in several respects from the applicable U.S. substantive law in this case. While the 10b-5 securities fraud claim in the U.S. action required a showing of knowledge or intent,<sup>184</sup> an issuer’s liability under Section 11 of the Securities Act of 1933

<sup>178</sup> Court filings, including the complaint (*Klageschrift*), are not accessible to the public in Germany, because they are deemed confidential. Researchers may obtain special permission from the judge and review court files on site. This was not possible during the writing of this Article, as the files had been transferred to the appeals court and were unavailable. In the following, I rely on published judicial decisions and orders in the case (which review the claims in great detail), news accounts, press releases, publications by and personal communications with plaintiff-side attorneys, as well as discussions of the case in the academic literature, which draw on all of the above.

<sup>179</sup> *Oberlandesgericht Frankfurt/Main* [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06, at 85ff, 113ff.

<sup>180</sup> *Börsengesetz* [BoersG] [Stock Exchange Law], July 16, 2007, *Bundesgesetzblatt Teil I* [BGBl I] at 1366, repealed Dec. 6, 2012, BGBl I at 248, §§ 44–45; *Bundesgerichtshof* [BGH] [Federal Court of Justice] May 31, 2011, *Neue Juristische Wochenschrift* 2719, 2011.

<sup>181</sup> See sources cited *supra* note 180; see also *Bürgerliches Gesetzbuch* [BGB] [Civil Code], § 823, ¶ 2, translation at [http://www.gesetze-im-internet.de/englisch\\_bgb/englisch\\_bgb.html#p3484](http://www.gesetze-im-internet.de/englisch_bgb/englisch_bgb.html#p3484) [[http://web.archive.org/web/20160416172619/https://www.gesetze-im-internet.de/englisch\\_bgb/englisch\\_bgb.html](http://web.archive.org/web/20160416172619/https://www.gesetze-im-internet.de/englisch_bgb/englisch_bgb.html)] (defining the civil law claim for damages); *Strafgesetzbuch* [StGB] [Penal Code], § 264, translation at [http://www.gesetze-im-internet.de/englisch\\_stgb/englisch\\_stgb.html#p2192](http://www.gesetze-im-internet.de/englisch_stgb/englisch_stgb.html#p2192) [<https://perma.cc/QTP7-8JPS>] (defining criminal subsidy fraud); Patrick S. Ryan, *Understanding Director & Officer Liability in Germany for Dissemination of False Information: Perspectives from an Outsider*, 4 *GERMAN L.J.* 439, 473 (2003) (discussing the applicable German laws related to liability arising from a false statement).

<sup>182</sup> *Börsengesetz* [BoersG] [Stock Exchange Law], July 16, 2007, *Bundesgesetzblatt Teil I* [BGBl I] at 1366, repealed Dec. 6, 2012, BGBl I at 248, § 44.

<sup>183</sup> *Id.* § 45.

<sup>184</sup> See 17 C.F.R. 240.10b-5 (2014).

for material mistakes or omissions in a registration statement admits of no defense and does not require a showing of negligence.<sup>185</sup>

This difference in substantive law might alone have accounted for the different outcomes in the United States and in Germany, but the German court never got to rule on the affirmative defense. Instead it decided the case by finding the prospectus was not materially false or misleading with regard to both the VoiceStream and real estate allegations.<sup>186</sup> Both the U.S. and German outcomes therefore turned on whether the prospectuses were materially false or misleading.

#### IV. DEVELOPMENT OF THE LITIGATION

##### A. *Development of the Litigation in the Southern District of New York*

In the Southern District of New York, the case proceeded fairly rapidly. The class action complaint in the original case was filed on December 13, 2000<sup>187</sup>—before Deutsche Telekom's February 2001 write-down of \$2 billion in real estate assets.<sup>188</sup> Judge Stein set the initial case management conference for January 26, 2001.<sup>189</sup> On March 22, 2001, the cases were consolidated before Judge Stein.<sup>190</sup> On April 11, 2001, the well-known plaintiff-side firms, Bernstein Liebhard & Lifshitz and Milberg Weiss were appointed as counsel to co-lead plaintiffs.<sup>191</sup> The Judge issued a scheduling order on July 16, 2001, requiring the first set of document requests to be served by July 27, 2001 and production of documents by September 28, 2001.<sup>192</sup> A year after the announcement of the VoiceStream merger, the cases had thus been consolidated and discovery commenced.<sup>193</sup>

KfW was dismissed from the case on February 20, 2002.<sup>194</sup> Judge Stein granted class certification shortly thereafter, on October 29, 2002.<sup>195</sup> Discovery lasted just over two years, with defendants repeatedly seeking extensions of discovery, especially with respect to the real estate issues.<sup>196</sup>

<sup>185</sup> Securities Act of 1933, ch. 38, § 11, 48 Stat. 74, 82 (codified as amended at 15 U.S.C. § 77k (2012)).

<sup>186</sup> Bundesgerichtshof [BGH] [Federal Court of Justice] May 31, 2011, *Neue Juristische Wochenzeitschrift* 2719, 2011.

<sup>187</sup> Docket, *In re Deutsche Telekom AG Sec. Litig.*, No. 00 CIV 9475 SHS, 2002 WL 244597 (S.D.N.Y. Feb. 20, 2002).

<sup>188</sup> *Deutsche Telekom Will Incur Charge for Real-Estate Holdings*, *supra* note 163.

<sup>189</sup> Docket, *supra* note 187.

<sup>190</sup> *Id.*

<sup>191</sup> *Id.*

<sup>192</sup> *Id.*

<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

<sup>195</sup> *In re Deutsche Telekom AG Sec. Litig.*, 229 F. Supp. 2d 277, 284 (S.D.N.Y. 2002).

<sup>196</sup> See Docket, *supra* note 187. The list of filings during the discovery phase can be found between docket entry numbers 62–74.

Plaintiffs took over thirty depositions and reviewed over 1.9 million documents.<sup>197</sup>

One week before the October 13, 2003 final discovery deadline, the investment banks and underwriters moved for summary judgment.<sup>198</sup> The parties exchanged memoranda on the motions for summary judgment, which were never filed.<sup>199</sup> The parties then took more than a year to negotiate a settlement and applied for judicial approval of a settlement on January 28, 2005.<sup>200</sup> The settlement required Deutsche Telekom to pay \$120 million to the plaintiffs' class fund.<sup>201</sup> The other defendants paid nothing (except perhaps their legal fees).<sup>202</sup> In the settlement, the defendants admitted to no wrongdoing.<sup>203</sup>

### B. Development of the German Litigation

In the Deutsche Telekom litigation, thousands of plaintiffs swamped the judiciary at the district court in Frankfurt (*Frankfurter Landesgericht*) to which the cases were assigned.<sup>204</sup> The plaintiffs in the German litigation were mostly retail investors who had purchased Deutsche Telekom shares subject to the German offering.<sup>205</sup> Total claims were around 100 million Euros, and the average claim was valued at around 5,900 Euros.<sup>206</sup> Because there were three Deutsche Telekom share issuances in Germany, but only one in the United States, the German litigation against Deutsche Telekom also involved claims relating to the real estate valuations of the earlier German prospectuses going back to 1996.<sup>207</sup> All told, 17,000 shareholders who purchased in these three issuances brought claims before the German regional court in Frankfurt by the end of 2003.<sup>208</sup> The large volume of cases overwhelmed the Frankfurt court. Because there was no class action mechanism, each case would have to be treated separately and tried separately.<sup>209</sup>

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<sup>197</sup> Stipulation and Agreement of Settlement at 5, *Deutsche Telekom*, 229 F. Supp. 2d 277 (No. 00-CV-9475), [http://securities.stanford.edu/filings-documents/1016/USD00/2005128\\_r04s\\_00CV9475.pdf](http://securities.stanford.edu/filings-documents/1016/USD00/2005128_r04s_00CV9475.pdf) [<https://perma.cc/ZS2P-HF9E>].

<sup>198</sup> *Id.* at 4.

<sup>199</sup> *Id.*; Telephone Interview with Robert Wallner, Counsel for Plaintiffs, Milberg LLP (Dec. 30, 2014).

<sup>200</sup> Stipulation and Agreement of Settlement, *supra* note 197, at 19.

<sup>201</sup> *Id.* at 11.

<sup>202</sup> *Id.*

<sup>203</sup> *Id.* at 22.

<sup>204</sup> Gorga & Halberstam, *supra* note 13, at 1488–89.

<sup>205</sup> *Id.*; Tilp, *supra* note 16, at 332–33.

<sup>206</sup> Tilp & Roth, *supra* note 9, at 132.

<sup>207</sup> German litigants referred to these three issuances as DT1 (1996), DT2 (1998), and DT3 (in June 2000). Tilp, *supra* note 16, at 332–33.

<sup>208</sup> *Id.* at 332.

<sup>209</sup> *Id.* at 332–33.

The first complaints were filed in late 2001.<sup>210</sup> But the court in Frankfurt did not hold its first hearing in the matter until November 11, 2004.<sup>211</sup> The hearing took place only after the German constitutional court (BGH) had weighed in on the lengthy delay in the process.<sup>212</sup> To handle the flood of cases, the Frankfurt regional court selected ten pilot cases that raised the most important issues for expedited proceeding.<sup>213</sup>

Note that, by this time, the U.S. parties had already long concluded discovery and were presumably negotiating a settlement. In Germany, by contrast, the plaintiffs had, at this point, received no information from the defendants, and the German court's interrogation of its first witness would have to wait another three-and-a-half years.<sup>214</sup> To overcome their lack of company internal information, attorneys for the German plaintiffs sought to benefit from the parallel proceedings in the United States.<sup>215</sup> They knew that the case there had progressed rapidly and was going through full discovery.<sup>216</sup> In January of 2003, they thus filed a petition pursuant to 28 U.S.C. § 1782 to obtain discovery produced in the U.S. litigation.<sup>217</sup>

### C. *The German Plaintiffs' Attempt to Obtain Evidence from Overseas*

28 U.S.C. § 1782 provides that a district court may direct that a person who resides or is found in the district "give his testimony or statement or . . . produce a document or other thing for use in a . . . foreign or international tribunal."<sup>218</sup> "The statute affords access to discovery of evidence in the United States for use in foreign proceedings."<sup>219</sup> The request may come from "any interested person."<sup>220</sup> But while the statute "authorizes" a judge to grant such discovery, it also gives judges broad discretion to, *inter alia*, consider the sovereignty interests of other countries in their own administration of justice.<sup>221</sup>

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<sup>210</sup> *Id.* at 332.

<sup>211</sup> *Id.* at 338–39.

<sup>212</sup> *Id.* at 345.

<sup>213</sup> *Id.*

<sup>214</sup> *Id.* at 314.

<sup>215</sup> Gorga & Halberstam, *supra* note 13, at 1490.

<sup>216</sup> *Id.*

<sup>217</sup> *Id.*; see also *Schmitz v. Bernstein Liebhard & Lifshitz, LLP*, 376 F.3d 79, 85 (2d Cir. 2004) (denying the petition for discovery).

<sup>218</sup> 28 U.S.C. § 1782 (2012).

<sup>219</sup> *In re Schmitz*, 259 F. Supp. 2d 294, 296 (S.D.N.Y. 2003) (quoting *In re Edelman*, 295 F.3d 171, 175 (2d Cir. 2002)).

<sup>220</sup> *Id.*

<sup>221</sup> See *In re Application for an Order for Judicial Assistance in a Foreign Proceeding in the High Court of Justice, Chancery Division, England*, 147 F.R.D. 223, 226 (C.D. Cal. 1993) ("The intent behind [28 U.S.C. § 1782] was to facilitate compliance by U.S. citizens with foreign court proceedings and to maintain respect for foreign countries' sovereign jurisdiction.").

The use of § 1782 is a topic of great interest to cross-border litigation in that it affords those who litigate in international tribunals or foreign countries a remarkable opportunity for obtaining information about a party-opponent that they would ordinarily be unable to obtain under non-U.S. procedural rules. There is a small but longstanding practice by European litigants to attempt to obtain discovery against party-opponents in the United States.<sup>222</sup>

In their § 1782 petition to Judge Stein in the S.D.N.Y., the German plaintiffs contended that the U.S. securities class action litigation then pending before the court had “substantially identical” allegations to the allegations in the German actions.<sup>223</sup> They sought to obtain all documents that had by that time been produced by Deutsche Telekom’s U.S. counsel, Cravath, Swaine & Moore, to the lead plaintiffs’ counsel, Milberg Weiss and Bernstein Liebhard & Lifshitz.<sup>224</sup> Milberg and Bernstein took no position as to the production of documents, but Deutsche Telekom objected, arguing they had conducted discovery in the U.S. action in reliance on a discovery confidentiality order.<sup>225</sup> More importantly, Deutsche Telekom cited strong objections by the German government and judiciary.<sup>226</sup>

In opposition to the petition of the German investors for access to the U.S. discovery materials, Cravath filed letters from the Bonn prosecutor and the German Ministry of Justice opposing the production on the grounds that it would compromise an ongoing criminal investigation into Deutsche Telekom’s real estate valuations.<sup>227</sup> The German authorities and experts for Cravath pointed out that German law prohibited sharing a prosecutor’s documents and files in an ongoing investigation because it would jeopardize the investigation and violate the privacy rights of the accused.<sup>228</sup> The German government also noted that the German plaintiffs had already requested the documents from the Bonn prosecutor, who had refused to grant such access for just this reason.<sup>229</sup> Allowing the German plaintiffs to obtain these documents from the United States would allow them to perform an end-run around the German judicial authorities, thus implicating German sovereignty interests.<sup>230</sup> According to the German

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<sup>222</sup> See generally Lauren Ann Ross, *A Comparative Critique to U.S. Courts’ Approach to E-Discovery in Foreign Trials*, 11 DUKE L. & TECH. REV. 313 (2012) (discussing jurisprudence governing this practice).

<sup>223</sup> *Schmitz*, 259 F. Supp. 2d at 296.

<sup>224</sup> *Id.*

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* at 298.

<sup>227</sup> *Id.* at 296.

<sup>228</sup> *Id.* at 299.

<sup>229</sup> *Id.* at 297.

<sup>230</sup> *Id.*

Ministry for Justice, the prosecutor's office would reconsider the German plaintiff's request for access to the documents at a later date.<sup>231</sup>

As mentioned above, the state prosecutor in Bonn had initiated a criminal investigation into Deutsche Telekom's valuation of its real estate transactions in connection with its securities issuances.<sup>232</sup> The investigations were terminated in the spring of 2005, with Deutsche Telekom entering a consent decree that required it to contribute five million Euros to charitable organizations.<sup>233</sup>

Following the conclusion of the criminal investigation, in May of 2005, the regional court in Bonn (LG) finally did afford plaintiffs limited access to the Bonn prosecutor's files.<sup>234</sup> Plaintiffs recounted that they received over fifty boxes of documents and files from the Bonn prosecutor's investigations into Deutsche Telekom's real estate valuations.<sup>235</sup> This was by far the largest trove of documents obtained by the German plaintiffs in support of their case.<sup>236</sup>

But it is also important to note that they would never have come into possession of these documents if there had been no criminal investigation of Deutsche Telekom's real estate valuations. Accordingly, the German plaintiffs were unable to obtain the vast majority of documents from Deutsche Telekom regarding the VoiceStream allegations, because these allegations were not the subject of a German criminal investigation.<sup>237</sup>

#### D. The "Deutsche Telekom" Law

The Deutsche Telekom litigation is frequently cited in the recent German literature as a prime example of the kind of "mass damages" litigation that calls for an aggregate litigation mechanism.<sup>238</sup> As already noted, over 17,000 claimants swamped the judiciary at the district court in Frankfurt.<sup>239</sup> The judicial system simply could not process such a large number of claims by adhering to civil procedure rules that were based on the German (civil law) model of a dispute between two parties.<sup>240</sup> And the

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<sup>231</sup> *Id.*

<sup>232</sup> *Id.* at 295.

<sup>233</sup> Tilp, *supra* note 16, at 353.

<sup>234</sup> *Id.* at 339.

<sup>235</sup> Interview with Andreas Tilp, named partner with TILP Rechtsanwaltsgesellschaft mbH, in Kirchentellinsfurt, Ger. (July 2015).

<sup>236</sup> *Id.*

<sup>237</sup> *Id.*

<sup>238</sup> André Janssen, *Auf dem Weg zu Einer Europäischen Sammelklage?*, in EUROPÄISCHEN SAMMELKLAGE, *supra* note 13, at 3, 5–6; KÖLNER KOMMENTAR, *supra* note 11, at 20.

<sup>239</sup> Gorga & Halberstam, *supra* note 13, at 1488–89.

<sup>240</sup> Tilp, *supra* note 16, at 333.

cases languished for three years without any hearings. Commentators spoke of a “collapse” of the judicial system.<sup>241</sup>

The German parliament responded by passing the “Capital Markets Model Procedure Act” (*Kapitalmusterverfahrensgesetz*, or “KapMuG”) to render the resolution of damages and rescission claims arising out of securities disclosure violations more efficient.<sup>242</sup> As a result of this close connection between the passage of KapMuG and the Deutsche Telekom litigation, KapMuG is also frequently referred to as the “Deutsche Telekom Law.”<sup>243</sup>

KapMuG, which became effective in November of 2005, provided for an experimental civil procedure limited to claims of securities disclosure violations.<sup>244</sup> In other words, it does not apply trans-substantively to consumer protection or antitrust claims, but was intended as a pilot project for the adjudication of mass claims that might be expanded to other substantive areas of the law in the future.<sup>245</sup> The law had a sunset provision that would expire in 2012 unless renewed by the German Parliament, which it was with certain amendments.<sup>246</sup>

The KapMuG procedure does not create a U.S.-type class action where claims are bundled in a pre-trial phase and then prosecuted (or settled) by a representative for the class. Rather, it keeps all claims separate, but tries common questions of law and fact in a “model proceeding” (*Musterverfahren*), which is binding as to the issues presented and resolved in that “model proceeding.”<sup>247</sup> Thus, there is no bundling of claims, but a bundling of issues common to a particular controversy (*Lebenssachverhalt*).<sup>248</sup> The KapMuG proceeding has three phases.

First, plaintiffs or defendants in an existing action may file applications for the initiation of a special model proceeding (*Musterverfahrens Antrag*/Model Proceeding Application) with the trial

<sup>241</sup> KÖLNER KOMMENTAR, *supra* note 11, at 30–31; Verse, *supra* note 40, at 451.

<sup>242</sup> ASSMANN & SCHÜTZE, *supra* note 40, §§ 44–46 (describing significance of KapMuG for private securities enforcement); André Janssen, *Auf dem Weg zu Einer Europäischen Sammelklage?*, in EUROPÄISCHEN SAMMELKLAGE, *supra* note 13, at 3, 6 (describing European goals for greater efficiency); Verse, *supra* note 40, at 451 (stating that the KapMuG procedure “aims at reducing the workload for the courts and the litigation costs for the parties”).

<sup>243</sup> ASSMANN & SCHÜTZE, *supra* note 40, § 44.

<sup>244</sup> Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act] Aug. 16, 2005, BGBl I at 243, § 1, translation at [http://www.gesetze-im-internet.de/englisch\\_kapmug/index.html](http://www.gesetze-im-internet.de/englisch_kapmug/index.html) [https://perma.cc/7BYT-HY6G].

<sup>245</sup> This generated criticism in the *Bundesrat* that investors were being afforded special procedural advantages. Fabian Reuschle, *Das Kapitalanleger-Musterverfahrensgesetz—Eine Erste Bestandsaufnahme aus Sicht der Praxis*, in EUROPÄISCHEN SAMMELKLAGE, *supra* note 13, at 277, 278 (describing the legislative debate about the need for a more efficient litigation process in connection with securities fraud).

<sup>246</sup> *Id.*

<sup>247</sup> KÖLNER KOMMENTAR, *supra* note 11, at 34–35.

<sup>248</sup> KapMuG § 4; KÖLNER KOMMENTAR, *supra* note 11, at 35, 230.



court.<sup>249</sup> If at least ten such applications are made (or ten or more joint parties make such application), then the trial court initiates a preparatory proceeding (*Vorlageverfahren*/Preparatory Proceeding), in which common questions of law and fact are identified and then compiled into a formal brief of questions and issues to be presented (*Vorlagebeschluß*/Brief of Questions Presented).<sup>250</sup> This special brief is then certified to a higher court (*Oberlandesgericht*) for decision.<sup>251</sup>

The second phase consists of the actual model proceeding (*Musterverfahren*/Model Proceeding) before the higher court.<sup>252</sup> In the Model Proceeding, the higher court essentially “tries” the issues or questions presented. Recall here that in civil law countries, courts of appeal are not limited to the record established in a trial court, but may take evidence under proper circumstances and need not defer to the factual findings of the court below.<sup>253</sup> The higher court then issues an opinion in the form of a set of “determinations” (*Feststellungen*) regarding the questions presented (*Musterentscheid*/Opinion Regarding Questions Presented).<sup>254</sup> During the time the model proceeding takes place, all related cases in the trial court are stayed.<sup>255</sup>

In the third phase, after the higher court has issued and published its Opinion Regarding Questions Presented, the individual actions that were stayed during the model proceeding are taken up again separately by the trial court and decided separately, based, in relevant part, on the determinations of the higher court in the Model Proceeding.<sup>256</sup> In other words, the higher court’s Opinion Regarding Questions Presented has an issue-preclusive effect.

In its application for a Model Proceeding, a party must establish that the issues proposed for resolution in the Model Proceeding represent common issues of law or fact in parallel actions currently pending.<sup>257</sup> Once the trial court receives a Model Proceeding Application from a party to an action, it must publish the application on its docket (*Klageregister*), upon which the individual action is automatically stayed.<sup>258</sup> The stay serves the KapMuG’s goal of increasing the efficiency of civil adjudication and conserving judicial resources, in that it avoids duplication of effort in evidence acquisition, fact-finding, and the determination of law in parallel

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<sup>249</sup> KapMuG § 2(1); KÖLNER KOMMENTAR, *supra* note 11, at 36.

<sup>250</sup> KapMuG § 6; KÖLNER KOMMENTAR, *supra* note 11, at 36–37.

<sup>251</sup> KapMuG § 6; KÖLNER KOMMENTAR, *supra* note 11, at 36–37.

<sup>252</sup> KapMuG § 6; KÖLNER KOMMENTAR, *supra* note 11, at 37.

<sup>253</sup> MURRAY & STÜRNER, *supra* note 22, at 609.

<sup>254</sup> KapMuG § 16; KÖLNER KOMMENTAR, *supra* note 11, at 496ff.

<sup>255</sup> KapMuG §§ 5, 8(1); KÖLNER KOMMENTAR, *supra* note 11, at 36, 245ff.

<sup>256</sup> KapMuG § 22; KÖLNER KOMMENTAR, *supra* note 11, at 38.

<sup>257</sup> KapMuG § 2.

<sup>258</sup> KapMuG §§ 3(2), 5; KÖLNER KOMMENTAR, *supra* note 11, at 245ff.

actions.<sup>259</sup> It falls to the trial court to determine whether the ten Model Proceeding Applications required to initiate a Model Proceeding, in fact, raise common issues of law or fact, and which questions or issues of law or fact are to be certified to the higher court.<sup>260</sup> The focus in this inquiry is whether the applications arise out of the same set of facts and circumstances (*Lebenssachverhalt*), roughly like the joinder and preclusion inquiries operate in federal court.<sup>261</sup>

The goal of this new aggregate procedure was to increase the efficiency with which mass claims would be disposed of. In *Deutsche Telekom*, for example, the resolution of common questions in a Model Proceeding would consolidate evidence acquisition and fact-finding in hundreds or thousands of individual cases, regarding the accuracy of Deutsche Telekom's prospectus.<sup>262</sup> But in so doing, the KapMuG also clashes with fundamental principles of German (and common law) civil procedure.

One such principle is that parties to a dispute should have overall control over the nature and scope of the civil litigation (*Dispositionsmaxime*), including its initiation, the issues presented, the relief requested, the presentation of evidence, and the termination of the suit.<sup>263</sup> The principle of party control is a fundamental principle of due process that permeates German and civil law procedure.<sup>264</sup> A corollary to this principle is the "Principle of Party Presentation" (*Beibringungsgrundsatz*), which provides that the parties themselves are responsible for determining the means of proof and identifying the evidence to support their claims or defenses.<sup>265</sup> While these principles seem consistent with federal procedure, their interpretation in the context of the civil law tradition results in markedly different rights and procedures.

The German principle of party control (*Dispositionsmaxime*) militates against full-fledged representative litigation as it is practiced in the U.S. class action.<sup>266</sup> The adjudication of common issues of law and fact in a representative proceeding that is preclusive for all class members,

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<sup>259</sup> KapMuG § 2(1); Fabian Reuschle, *Das Kapitalanleger-Musterverfahrensgesetz—Eine Erste Bestandsaufnahme aus Sicht der Praxis*, in *EUROPÄISCHEN SAMMELKLAGE*, *supra* note 13, at 277, 278–79.

<sup>260</sup> See KapMuG §§ 3(1), 6 (discussing the circumstances under which the court trying the matter will deny the application as inadmissible and the procedure of reference to the Higher Regional Court).

<sup>261</sup> Fabian Reuschle, *Das Kapitalanleger-Musterverfahrensgesetz—Eine Erste Bestandsaufnahme aus Sicht der Praxis*, in *EUROPÄISCHEN SAMMELKLAGE*, *supra* note 13, at 277, 278–79.

<sup>262</sup> *Id.* at 278.

<sup>263</sup> MURRAY & STÜRNER, *supra* note 22, at 154–56. This principle is also referred to as the "party principle" (*Parteiprinzip*).

<sup>264</sup> *Id.* at 156.

<sup>265</sup> KUO-CHANG HUANG, *INTRODUCING DISCOVERY INTO CIVIL LAW* 21–22 (2003).

<sup>266</sup> KÖLNER KOMMENTAR, *supra* note 11, at 60.

including those who never agreed to join the proceedings, is anathema to the German right to control one's own case presentation. The KapMuG thus eschews full-fledged representative litigation and keeps individual cases separate, even as it resolves shared questions of law and fact in the Model Proceeding—but it does so at a cost to efficiency. Moreover, the Model Proceeding does not bind non-litigants, thus distinguishing itself from the U.S. opt-out model.<sup>267</sup>

Nonetheless, at least two structural features of the KapMuG have raised constitutional concerns.

First, the trial judge's substantial influence on generating the Brief of Questions Presented, which is then submitted for litigation to the higher court, involves a level of judicial control over the presentation of the issues in the case that sits uncomfortably with the principle of party control.<sup>268</sup>

Second, the KapMuG's selection of a few "test cases" that will be litigated and will generate determinations binding on all the parties still contravenes the principle of party presentation. Under the original statute, parties not selected to participate in the Model Proceeding had limited (or no) influence on the presentation of facts in a proceeding that could have a decisive influence on the outcome in their own cases.<sup>269</sup> The courts have responded to this due process issue by giving the other parties the status of intervenors, with a right to present evidence in the Model Proceeding as well, thus mitigating the concern that they will be bound by proceedings in which they had no voice.<sup>270</sup>

Generally speaking, however, the KapMuG proceeding is subject to all of the standard procedural requirements of the German civil procedure code,<sup>271</sup> which, as we shall see, imposes substantial limitations on the parties' (and especially the plaintiffs') ability to engage in fact investigation.

#### E. *The Deutsche Telekom KapMuG Proceeding*

In December of 2005, shortly after the effective date of KapMuG, plaintiffs in one of the pilot cases filed their application for a model proceeding.<sup>272</sup> Others soon followed.<sup>273</sup> The lower Frankfurt Regional

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<sup>267</sup> *Id.* at 40–41.

<sup>268</sup> *Id.* at 60–61, 297.

<sup>269</sup> *Id.* at 62.

<sup>270</sup> *Id.* at 66–67; Tilp, *supra* note 16, at 355.

<sup>271</sup> KÖLNER KOMMENTAR, *supra* note 11, at 60.

<sup>272</sup> Landesgericht Frankfurt/Main [LG Frankfurt/Main] [Regional Court Frankfurt/Main], July 19, 2006, 3/07 OHG 1/06; Tilp, *supra* note 16, at 347. Winkler is the "model claimant" challenging the June 1999 share offering (DT2), regarding, *inter alia*, the real estate valuations in the DT2.

<sup>273</sup> In the following, I rely on decisions in the case of Kiefer against Deutsche Telekom, because Kiefer is the "model claimant" that challenges the June 2000 share offering (DT3) regarding, *inter alia*, the real estate valuations and the VoiceStream acquisition. Landesgericht Frankfurt/Main [LG

Court drafted a 193-page Brief of Questions Presented, including thirty-three questions or issues for resolution by the Higher Regional Court.<sup>274</sup> The 193-page brief, which was published on July 11, 2006, included references to documents, affidavits, and witnesses that each side would rely on to make its case. The brief was worked out in a preparatory proceeding based on written submissions by the various parties and negotiations as to what could be stipulated.<sup>275</sup> The parties' written submissions were supported by evidence submitted to the court, including expert assessments of Deutsche Telekom's real estate valuations.<sup>276</sup>

On July 25, 2006, the Higher Regional Court chose the "model claimant" (or perhaps lead plaintiff) for the claims arising out of the June 2000 offering.<sup>277</sup> But evidentiary hearings would not begin until April 14, 2008.<sup>278</sup> The delay was in part due to amendments to the Brief of Questions Presented sought by the parties.<sup>279</sup> In the meantime, the lower court encountered difficulties adjudicating which of the thousands of cases would be stayed pending the outcome of the model proceedings—a laborious and time-consuming process.<sup>280</sup> This process took nearly one year, because the lower court had to make a separate determination for each case.<sup>281</sup> Those litigants would enjoy the status of intervenors in the model proceeding. Due process concerns about the right of the "intervenors" (*beigeladene*) to a fair hearing resulted in an order by the

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Frankfurt/Main] [Regional Court Frankfurt/Main], Dec. 4, 2006, 3/7 OH 1/06. As noted above, court filings, including complaints, are not publicly available. The KapMuG, however, does require certain court filings in the Model Proceeding to be made available to all claimants with related claims by posting them on a website. *But see* Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act] Aug. 16, 2005, BGBl I at 243, § 4(4), *translation at* [http://www.gesetze-im-internet.de/englisch\\_kapmug/index.html](http://www.gesetze-im-internet.de/englisch_kapmug/index.html) [<https://perma.cc/7BYT-HY6G>] (requiring Model Proceeding Applications to be deleted upon final decision in the Model Proceeding). Certain judicial decisions, to which I refer below, are publicly available.

<sup>274</sup> Landesgericht Frankfurt a.M. [LG Frankfurt/M] [Frankfurt Regional Court], July 11, 2006, 23 Kap 1/06, 3/7 OH 1/06; KÖLNER KOMMENTAR, *supra* note 11, at 58–59; Tilp & Roth, *supra* note 9, at 136.

<sup>275</sup> Landesgericht Frankfurt a.M. [LG Frankfurt/M] [Frankfurt Regional Court], July 11, 2006, 23 Kap 1/06, 3/7 OH 1/06; *see also* KapMuG § 6(1)–(2); KÖLNER KOMMENTAR, *supra* note 11, at 258–67, 274–79. The proceeding is typically based on written submissions.

<sup>276</sup> These are discussed in the Brief of Questions Presented, LG Frankfurt/Main, Vorlagebeschluß, Landesgericht Frankfurt a.M. [LG Frankfurt/M] [Frankfurt Regional Court], July 11, 2006, 23 Kap 1/06, 3/7 OH 1/06.

<sup>277</sup> Tilp, *supra* note 16, at 339.

<sup>278</sup> *Id.* at 356.

<sup>279</sup> KÖLNER KOMMENTAR, *supra* note 11, at 58; Tilp, *supra* note 16, at 352; AXEL HALFMEIER ET AL., EVALUATION DES KAPITALANLEGER-MUSTERVERFAHRENSGESETZES 28 (2009), <http://docplayer.org/1360128-Evaluation-des-kapitalanleger-musterverfahrensgesetzes.html> [<https://perma.cc/GX3N-RPV9>].

<sup>280</sup> Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act] Aug. 16, 2005, BGBl I at 243, § 7, *translation at* [http://www.gesetze-im-internet.de/englisch\\_kapmug/index.html](http://www.gesetze-im-internet.de/englisch_kapmug/index.html) [<https://perma.cc/7BYT-HY6G>]; Tilp, *supra* note 16, at 352.

<sup>281</sup> HALFMEIER ET AL., *supra* note 279, at 28.

Higher Regional Court to grant parties the right to actively participate in the model proceeding and give the attorneys for all of the parties access to all the pleadings and briefs on a password-protected website.<sup>282</sup> This is of interest, because it introduced a level of publicity into the proceedings that is ordinarily not contemplated by German civil procedure.<sup>283</sup>

Hearings before the Higher Regional Court began on April 4, 2008.<sup>284</sup> Thirteen full days of hearings were held during April and May during which the court heard testimony from sixteen witnesses, mostly executives of the defendant Deutsche Telekom.<sup>285</sup>

An important victory for the plaintiffs was a decision by the court to order the Deutsche Telekom defendants to produce transcripts of four of the depositions that were taken in the U.S. litigation.<sup>286</sup> These depositions became part of the record, and were relied on, *inter alia*, as corroborating evidence by the German court.<sup>287</sup> The court also required the defendants to produce some of the exhibits U.S. plaintiffs' counsel had obtained in discovery and used to interrogate the deponents in the U.S. action.<sup>288</sup> The German plaintiffs (and the court) were thus afforded access to at least some of the emails and electronic data relating to their VoiceStream claims—documents which they would not have been able to obtain under German procedural rules.

It is worth noting that the German plaintiffs were able to obtain the depositions by judicial order only because they knew that these documents were in the possession of the defendant Deutsche Telekom and knew what they contained based on information they had about the U.S. proceedings. The principle of presentation (*Beibringungsmaxime*) requires each party to provide proof to support its own claims and defenses.<sup>289</sup> As Huang has noted, this “makes it perfectly appropriate and legitimate for a party to hold back adverse material that has decisive bearing on the outcome of the litigation, and to obtain victory simply because his opponent has no access

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<sup>282</sup> KapMuG §§ 4, 6; Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], Sept. 25, 2007, 23 Kap. 1/06; Tilp, *supra* note 16, at 355.

<sup>283</sup> Unlike court filings in the United States, briefs to the court are not accessible to the public in Germany, but court administration does have discretion to provide access to such material upon special request to legal scholars for research purposes.

<sup>284</sup> Tilp, *supra* note 16, at 340.

<sup>285</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06, at 73 (paginated original on file with author); Tilp, *supra* note 16, at 340–41, 356–57.

<sup>286</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], Aug. 6, 2008, 23 Kap 1/06 (requiring Deutsche Telekom to produce depositions of Sommer, Eick, Hedberg, and (relevant portions of) the deposition of Ricke); Tilp, *supra* note 16, at 340–41, 356–57.

<sup>287</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06, at 85–104.

<sup>288</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], Aug. 6, 2008, 23 Kap 1/06.

<sup>289</sup> HUANG, *supra* note 265, at 21–22; MURRAY & STÜRNER, *supra* note 22, at 263–64.

to that material.”<sup>290</sup> A party-opponent generally cannot be forced to produce documentary evidence to support a party’s claims or defenses under civil law, except under very limited circumstances, and then only by order of the court.<sup>291</sup> At best a party may make a request for an order to produce “a document” (referred to in the code in the singular), and the request “must identify the document requested with reasonable specificity, describe its relevance to some fact in issue, and set forth the basis for the belief that it is in the possession or control of the opponent.”<sup>292</sup> Blanket requests for “all documents relating to . . .”—as is typical of a Request for the Production of Documents and Things Under the Federal Rules of Civil Procedure—are not contemplated.<sup>293</sup>

The German court took another four years to issue its main decision in the model proceeding. The opinion, ruling in favor of Deutsche Telekom on both the VoiceStream allegations and real estate valuation issues, was published on May 16, 2012 and is 184 pages long.<sup>294</sup> I discuss the opinion in detail in Part V below. It is worth noting the unusual length and factual detail of the opinion, which stands out amidst the typically concise summary opinions of no more than a few pages that German courts usually issue.

After the Regional Court in Frankfurt issued its opinion in the Model Proceedings, plaintiffs appealed to the German Federal Court in Karlsruhe (*Bundesgerichtshof*).<sup>295</sup> During the appeal the individual cases remained

<sup>290</sup> HUANG, *supra* note 265, at 27.

<sup>291</sup> In the nineteenth century, U.S. common law adhered to the same principle and only courts of equity could obtain information from a party-opponent, which required a bill in equity. Stephen N. Subrin, *How Equity Conquered Common Law: The Federal Rules of Civil Procedure in Historical Perspective*, 135 U. PA. L. REV. 909, 918, 929 (1987). This changed with the “discovery revolution” initiated by the passage of the Federal Rules of Civil Procedure in 1937 and its subsequent development up until the 1970s. See Gorga & Halberstam, *supra* note 13, at 1406–09, 1415 (discussing the creation of the Federal Rules of Civil Procedure, which emphasized the importance of an extended discovery period to facilitate broad fact investigation by both parties).

<sup>292</sup> MURRAY & STÜRNER, *supra* note 22, at 277; see also Zivilprozeßordnung [ZPO] [civil procedure statute] Dec. 5, 2005, Bundesgesetzblatt [BGBl] I at 3202, §§ 421–24, *translation at* [http://www.gesetze-im-internet.de/englisch\\_zpo/englisch\\_zpo.html#p1645](http://www.gesetze-im-internet.de/englisch_zpo/englisch_zpo.html#p1645) [[http://web.archive.org/web/20160305135918/https://www.gesetze-im-internet.de/englisch\\_zpo/englisch\\_zpo.html](http://web.archive.org/web/20160305135918/https://www.gesetze-im-internet.de/englisch_zpo/englisch_zpo.html)] (stating that if a party tendering evidence alleges that a document is held by the other party, they can file a petition that the court direct the other party to produce the document).

<sup>293</sup> It was only in 2001 that the German Civil Code was amended to include “relevance” as a basis for obtaining a document from a party opponent. Prior to that it was required that a party show it had an independent legal right to the possession or use of the document. MURRAY & STÜRNER, *supra* note 22, at 277–78.

<sup>294</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap. 1/06.

<sup>295</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&nr=69675&pos=0&anz=1> [<https://perma.cc/EJ67-67NY>]. The *Bundesgerichtshof* serves as a type of Federal Supreme Court for non-constitutional issues.

suspended. Plaintiffs declined to appeal the Regional Court's decision on the VoiceStream allegations because they felt they had insufficient evidence on this count.<sup>296</sup> They did, however, appeal the Regional Court's decision that Deutsche Telekom's offering properly disclosed the value of its real estate assets.<sup>297</sup>

In addition, the plaintiffs appealed a third issue, which was not accorded as much attention in the KapMuG proceedings or the U.S. litigation. The third issue was whether Deutsche Telekom had properly accounted for the sale of its holdings in the U.S. telecommunications company Sprint to one of Deutsche Telekom's affiliates.<sup>298</sup> Deutsche Telekom had booked the transaction as a sale, but the German plaintiffs claimed that the transaction was merely a transfer within Deutsche Telekom's group of affiliated businesses.<sup>299</sup> It took another two years, until October 12, 2014, for the federal panel to render its decision.<sup>300</sup> After thirteen years of litigation, the case is not over. The Federal Supreme Court affirmed the Higher Court's ruling that Deutsche Telekom's overvaluation of its real estate assets did not rise to the level of materiality.<sup>301</sup> But it reversed as to the accounting for the Sprint shares and held that the June 2000 prospectus was materially false in this regard.<sup>302</sup> This unexpected decision means that the lower courts must at the very least now contend with the issues of damages and causation, and potentially litigate the question of fault.<sup>303</sup>

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<sup>296</sup> Interview with Andreas Tilp, *supra* note 235.

<sup>297</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Sept. 18, 2012, Entscheidungen des Bundesgerichtshofes in Zivilsachen [BGHZ] 10607.

<sup>298</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&nr=69675&pos=0&anz=1> [https://perma.cc/EJ67-67NY].

<sup>299</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06, at 163ff; Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, at 37, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&nr=69675&pos=0&anz=1> [https://perma.cc/S26M-N7S7].

<sup>300</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&nr=69675&pos=0&anz=1> [https://perma.cc/5AQH-Y3DV].

<sup>301</sup> *Id.*

<sup>302</sup> *Id.*

<sup>303</sup> Bundesgerichtshof [BGH] [Federal Court of Justice], Oct. 21, 2014, XI ZB 12/12, at 49, <http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&nr=69675&pos=0&anz=1> [https://perma.cc/EAM2-ML7M]. Recall that liability for mistakes in an offering under Sections 44–45 of the Börsengesetz is not as strict as it is under Section 11 of the Securities Act of 1933, but affords defendants the affirmative defense that they did not act negligently or acted with ordinary negligence. Only gross negligence results in liability under German law, but the burden of proof is on the defendant.

## V. SUBSTANTIVE LAW APPLIED TO THE FACTS

The most viable claims against Deutsche Telekom, both in the United States and in Germany, were that the issuer had sold securities subject to a materially false or misleading registration statement and prospectus.

As previously noted, Section 11 of the Securities Act of 1933 subjects an issuer to strict liability for false or misleading statements in a prospectus, an extraordinary provision considering comparable common law tort standards.<sup>304</sup> The main issue for claims under Section 11 is whether the registration statement is materially false or misleading. Similarly, the issue on which the German court decided the Deutsche Telekom case was whether the prospectus was “materially” false or misleading. In the following, I discuss how “materiality” is interpreted under U.S. and German law.

A. *Materiality*

In the United States, “materiality” is defined in terms of what a “reasonable investor” would “with substantial likelihood” have considered important in making an investment decision.<sup>305</sup> The standard is fact intensive and depends upon the ability of plaintiffs to obtain discovery.<sup>306</sup> The leading case on the definition of “materiality,” *Basic v. Levinson*, is on point. In *Basic*, the Supreme Court considered whether Basic Incorporated’s statements concerning a merger were materially false or misleading.<sup>307</sup> The management of Basic had denied three times, over the course of two years, that it was in merger talks with Combustion Engineering.<sup>308</sup> The last denial occurred within eight weeks of Basic’s announcement that its board had endorsed Combustion Engineering’s tender offer.<sup>309</sup> In that context, the Supreme Court rejected the bright-line standard proposed by the defendants that a merger must be disclosed only after the merger partners have executed an agreement in principle.<sup>310</sup> Instead, the Court held that a fact-finder’s determination as to whether disclosure of a contingent future event, like a merger, was material depended on “whether the ‘reasonable investor’ would have considered the omitted information significant at the time.”<sup>311</sup>

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<sup>304</sup> Securities Act of 1933, ch. 38, § 11(a), 48 Stat. 74, 82 (codified as amended at 15 U.S.C. § 77k (2012)).

<sup>305</sup> *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (citing *TSC Indus. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

<sup>306</sup> *Id.* at 236, 240.

<sup>307</sup> *Id.* at 224.

<sup>308</sup> *Id.*

<sup>309</sup> *Id.* at 227, 228.

<sup>310</sup> *Id.* at 232, 233.

<sup>311</sup> *Id.* at 232.



In this canonical decision, the Court thus took the *TSC Industries*<sup>312</sup> “total mix of information” standard, applied it in the merger context, and extended it to Rule 10b-5 securities fraud actions generally.<sup>313</sup> In *TSC Industries*, the Supreme Court held that a fact is material if there is “a substantial likelihood that the . . . fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.”<sup>314</sup> Determinations of materiality, according to the *TSC Industries* Court, required “delicate assessments of the inferences a ‘reasonable shareholder’ would draw from a given set of facts and the significance of those inferences to him.”<sup>315</sup> This makes the inquiry into materiality fact intensive.

The German equivalent of “material” in Section 44(1) of the Stock Exchange Act (which applied at the time) is the term *wesentlich*.<sup>316</sup> German materiality also focuses on the investor and asks whether the investor received an appropriate (*zutreffendes*) picture (*Bild*) of the investment, and whether the prospectus accurately and completely informed the investor about all circumstances that are or could be material to the investor’s decision.<sup>317</sup> “A statement is considered material for liability purposes if it is more likely than not that a reasonable investor would take it into account when making his investment decision.”<sup>318</sup> While this formulation clearly tracks the U.S. standard of materiality, the application of the German materiality standard avoids an open-ended judicial assessment of what may or may not have been a reasonable investor response, in favor of fixed, so-called objective standards.

### B. Materiality in the Merger Context

In the merger context, where the fact-finder must determine whether a contingent future event should have been disclosed, the *Basic* Court gave additional guidance as to how the “reasonable investor” standard should be interpreted. The Court held that “[u]nder such circumstances, materiality ‘will depend at any given time upon a balancing of both the indicated

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<sup>312</sup> *TSC Indus. v. Northway, Inc.*, 426 U.S. 438 (1976).

<sup>313</sup> *Basic Inc.*, 485 U.S. at 231–32 (citing *TSC Indus.*, 426 U.S. at 449).

<sup>314</sup> *TSC Indus.*, 426 U.S. at 449; see also *Basic Inc.*, 485 U.S. at 224 (describing the standard for materiality as set forth in *TSC Industries*, whereby an omitted fact is material if there is a substantial likelihood that its disclosure would have been considered significant by a reasonable investor).

<sup>315</sup> *TSC Indus.*, 426 U.S. at 450.

<sup>316</sup> WOLFGANG GROB, KAPITALMARKTRECHT 188–89 (2006). As of June 2012, Sections 21–25 of the Act (*Prospektgesetz*) replaced Sections 44–47 of the Stock Exchange Act (*Börsengesetz*) and Sections 13–13a of the Sales Act (*Verkaufsprospektgesetz*). Verse, *supra* note 40, at 419 n.25.

<sup>317</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, at 46, 87–88 (citing decisional law and literature).

<sup>318</sup> Verse, *supra* note 40, at 419–20 (citing Bundesgerichtshof [BGH] [Federal Court of Justice], Sept. 18, 2012, Entscheidungen des Bundesgerichtshofes in Zivilsachen [BGHZ] 195).

probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity.”<sup>319</sup>

The assessment of the magnitude of a transaction is relatively straightforward in the merger context. In the Deutsche Telekom case, the \$50 billion acquisition of VoiceStream, representing around 50% of Deutsche Telekom’s asset value—which ranged from \$94 billion as of December 31, 1999 to \$124 billion as of December 31, 2000—clearly represented a transaction of sufficient magnitude to warrant disclosure.<sup>320</sup> Separately, Deutsche Telekom also had a duty to disclose, because it was issuing securities subject to a new registration statement.<sup>321</sup>

The key question for establishing Section 11 liability, based on the VoiceStream allegations, would thus have been the probability that the acquisition would be concluded.<sup>322</sup> In other words, how advanced were the merger negotiations at the time of the global offering? This question, indeed, was also the focus of the German court’s discussion as to whether Deutsche Telekom had properly disclosed its acquisition activity in the German prospectus.<sup>323</sup>

Based on the allegations in the amended complaint, the interest in the merger was present at the highest levels of management as of March 2000. Ron Sommer had had several phone calls with Mark Stanton, the VoiceStream CEO.<sup>324</sup> The management teams had met to explore the numbers in the Spring of 2000.<sup>325</sup> Deutsche Telekom made at least two offers to VoiceStream in June of 2000, one on June 6, the other on June 15.<sup>326</sup> Negotiations about price led Deutsche Telekom to increase its offer to \$200 per share—the final price that Deutsche Telekom paid for the VoiceStream shares.<sup>327</sup> And towards the end of June, Deutsche Telekom began its due diligence.<sup>328</sup> The commitment to the deal, the structure of the

<sup>319</sup> *Basic Inc.*, 485 U.S. at 238 (citing *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2d Cir. 1968)).

<sup>320</sup> See SEC. & EXCH. COMM’N, STAFF ACCOUNTING BULLETIN NO. 99—MATERIALITY (1999), <https://www.sec.gov/interps/account/sab99.htm> [<https://perma.cc/JQ73-UT34>] (recognizing that thresholds of five to ten percent have been used by auditors as a “rule of thumb,” but cautioning against the use of a simple quantitative approach); Deutsche Telekom AG, Annual Report for Fiscal Year ending Dec. 31, 2000 (Form 20-F), at app. F3 (May 4, 2001).

<sup>321</sup> See Securities Act of 1933, ch. 38, § 11(a), 48 Stat. 74, 82 (codified as amended at 15 U.S.C. § 77k (2012)) (providing that any person may sue when any part of the registration statement contained an untrue statement regarding a material fact, or failed to state a material fact, or was necessary to make the statements not misleading).

<sup>322</sup> See *Basic Inc.*, 485 U.S. at 238–39.

<sup>323</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06, at 87ff.

<sup>324</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 33(a)–(c).

<sup>325</sup> *Id.* ¶ 33(a), (b).

<sup>326</sup> *Id.* ¶ 33(c), (d).

<sup>327</sup> *In re Deutsche Telekom AG Sec. Litig.*, 229 F. Supp. 2d 277, 279 (S.D.N.Y. 2002).

<sup>328</sup> *Id.*

deal, and the price range would appear to have been available for disclosure when the June 16 securities issuance was sold.

Because the U.S. case was settled, discovery proceeded subject to a confidentiality agreement, and motions for summary judgment were never filed, our ability to assess the merits of plaintiffs' case is limited. We thus do not have access to documents, emails, or depositions in the U.S. case either directly or indirectly through exhibits or discussions of facts in briefs or opinions. What we do have is an unusually detailed and lengthy Opinion Regarding Questions Presented in the Model Proceeding by the German *Oberlandesgericht* in Frankfurt, which references key documents and depositions from the U.S. case. The new KapMuG statute indeed appears to have contributed to this unusually detailed discussion of facts on the record by the German court. The choice of test cases, which would include all of the central issues shared by registered claimants; the thorough preparation of the issues raised and the evidence to be presented at the trial court level; and the regional court's effort to make sure that the Model Proceeding would serve to resolve as many issues as possible, resulted in an unusually comprehensive and detailed discussion and finding of facts in the resulting opinion. Here we can use this information in the German opinion to reconstruct at least some of the evidence and arguments that would have been developed by the Deutsche Telekom defendants in the U.S. case to support a finding that the merger was not yet sufficiently probable at the time that the U.S. Registration Statement was filed, or at the time that the final prospectus was issued.

The German higher regional court heard eighteen witnesses, including the senior management of Deutsche Telekom and VoiceStream, but also frequently referenced the U.S. deposition transcripts that the court obtained by order from Deutsche Telekom.<sup>329</sup>

Deutsche Telekom's Chief Executive Officer Ron Sommer testified that all of the discussions with VoiceStream, up until the middle of July 2000, were primarily aimed at developing and maintaining Deutsche Telekom's contacts with VoiceStream in the context of an active and competitive market for firms in the telecommunications industry.<sup>330</sup> During the first six months of 2000, VoiceStream, Qwest, Sprint, and Nextel were all in sale-of-company (or substantial investment) negotiations with Deutsche Telekom's various suitors.<sup>331</sup> By June of 2000, VoiceStream had received several offers from third parties.<sup>332</sup> As late as July 25, 2000,

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<sup>329</sup> *Oberlandesgericht Frankfurt/Main* [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, at 73, 90 (referencing Sommer deposition); *id.* at 99 (referencing Hedberg and Stanton depositions).

<sup>330</sup> *Id.* at 97, 99.

<sup>331</sup> *Id.* at 98.

<sup>332</sup> *Id.* at 94.

VoiceStream was still engaged in parallel negotiations with the European company Orange.<sup>333</sup> This is corroborated by the joint proxy statement that Deutsche Telekom and VoiceStream filed with the SEC on July 25, 2000.<sup>334</sup> According to Sommer and others, Deutsche Telekom's engagement with VoiceStream from March through mid-July, including Deutsche Telekom's offers dated June 6, June 22, and July 5 of 2000, was aimed at retaining a seat at the table in the negotiations between VoiceStream and other suitors.<sup>335</sup> Deutsche Telekom board members testified that the decision to enter into an agreement with VoiceStream was made only on July 23, 2000, more than four weeks after Deutsche Telekom's June 19 share issuance.<sup>336</sup>

According to Sommer and several other witnesses, Deutsche Telekom was most interested in a deal with Qwest up until mid-July because a deal with Qwest would have best advanced Deutsche Telekom's overall global expansion strategy.<sup>337</sup> Deutsche Telekom's global expansion strategy was to find an acquisition target that would further more than one of Deutsche Telekom's five lines of business.<sup>338</sup> Qwest satisfied these requirements, but VoiceStream, which operated primarily as a wireless telecommunications provider, did not.<sup>339</sup> An acquisition or investment with Qwest was therefore the focus of Deutsche Telekom's U.S. expansion activities until July of 2000.<sup>340</sup> Only after it became evident that an agreement with Qwest would not be reached, during a July 12, 2000 meeting in Salt Lake City between Deutsche Telekom executives (including Sommer) and Qwest's Chairman of the Board, did Deutsche Telekom prioritize merger negotiations with VoiceStream.<sup>341</sup>

According to the German court, the testimony of Deutsche Telekom and VoiceStream executives was consistent with the timing of the negotiations that led to the July 23 agreement-in-principle.<sup>342</sup> Testimony by Stanton, VoiceStream's Chairman of the Board, confirmed that VoiceStream regarded an offer of \$200 per share as a precondition to any serious negotiations.<sup>343</sup> Other suitors had already offered \$200 a share.<sup>344</sup> Deutsche Telekom's June 22 offer of \$200 per share was therefore merely a condition for participating in further negotiations and did not represent an

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<sup>333</sup> *Id.*

<sup>334</sup> *Id.*

<sup>335</sup> *Id.* at 95–97, 99–100.

<sup>336</sup> *Id.* at 92.

<sup>337</sup> *Id.* at 90.

<sup>338</sup> *Id.* at 89.

<sup>339</sup> *Id.* at 89–90.

<sup>340</sup> *Id.* at 90.

<sup>341</sup> *Id.* at 90–91, 93.

<sup>342</sup> *Id.* at 95–96.

<sup>343</sup> *Id.*

<sup>344</sup> *Id.* at 99.

agreement.<sup>345</sup> As a result of its June 22 offer, Deutsche Telekom was permitted to send a team to Seattle (VoiceStream's headquarters) to conduct initial due diligence towards the end of June.<sup>346</sup> Plaintiffs cited this as evidence that an agreement had already been reached between VoiceStream and Deutsche Telekom.<sup>347</sup> But the German court credited the testimony of Deutsche Telekom executives and others that such preliminary due diligence was common to establish a proper valuation of the target and that Deutsche Telekom had conducted similar due diligence with Qwest, Nextel, and Cable Wireless, all of which were of interest to Deutsche Telekom as potential investments.<sup>348</sup>

Under U.S. law, the question as to whether the advanced merger negotiations should have been disclosed would have gone to a jury.<sup>349</sup> And we do not know what other facts a U.S. jury would have had available as a basis to conclude that the advanced merger negotiations were material and should have been disclosed. According to *Basic*, the jury would have had to engage in the following inquiry:

Generally, in order to assess the probability that the event will occur, a factfinder will need to look to indicia of interest in the transaction at the highest corporate levels. Without attempting to catalog all such possible factors, we note by way of example that board resolutions, instructions to investment bankers, and actual negotiations between principals or their intermediaries may serve as indicia of interest. . . . No particular event or factor short of closing the transaction need be either necessary or sufficient by itself to render merger discussions material.<sup>350</sup>

Under German law, the application of the materiality standard in the merger context is more rigid and favorable to the defendants. A merger need not be disclosed until a company's board (the German supervisory board or *Aufsichtsrat*) has adopted an agreement-in-principle.<sup>351</sup> This contrasts with the U.S. probability/magnitude standard, which does not require that an agreement-in-principle be executed.<sup>352</sup> According to the German agreement-in-principle standard, and based on the facts already

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<sup>345</sup> *Id.*

<sup>346</sup> *Id.* at 100.

<sup>347</sup> *Id.* at 103–04.

<sup>348</sup> *Id.* at 97–98.

<sup>349</sup> See *Basic Inc. v. Levinson*, 485 U.S. 224, 239 (1988) (“Whether merger discussions in any particular case are material therefore depends on the facts.”); see also Consolidated Amended Class Action Complaint, *supra* note 1 (demanding a jury trial).

<sup>350</sup> *Basic Inc.*, 485 U.S. at 239.

<sup>351</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, at 88.

<sup>352</sup> *Basic Inc.*, 485 U.S. at 238.

discussed, the German court thus found that the June 17 prospectus was not materially false or misleading because the supervisory board only voted to go forward with the merger on July 23, 2000, and no disclosure was required before this date.<sup>353</sup>

### C. *Materiality in the Real Estate Context*

Deutsche Telekom's February 21, 2001 write-down of \$2 billion to account for a decline in the value of its real estate assets came after serious questions about how the company had valued its real estate assets. As already noted, a German prosecutor in Bonn had already initiated a fraud investigation into Deutsche Telekom's real estate valuations in June of 2000. The investigation reflected profound concerns on the part of the former head of the real estate division of Deutsche Telekom, who departed from Deutsche Telekom because he considered the valuations to be fraudulent.

In and of itself, however, the February 2001 write-down did not concede that the real estate valuations had been false or misleading, or that they were material to investors. The company did not restate its financials, nor did it file a special 8k disclosure with the SEC. Instead, it merely reduced the carrying value of its real estate assets on its balance sheet by reassessing their value in 2001 in light of purportedly changed circumstances in the real estate markets.<sup>354</sup>

SEC Staff Bulletin No. 99 sets forth the SEC's interpretation of materiality for accounting purposes.<sup>355</sup> It recognizes that accountants make use of a rule of thumb that a "misstatement or omission of an item that falls under a 5% threshold is not material in the absence of particularly egregious circumstances."<sup>356</sup> Deutsche Telekom's real estate write-down represented less than five percent of the total balance sheet assets of Deutsche Telekom. So the five percent threshold was not reached.

But the Staff Bulletin rejects any purely quantitative measure of materiality. Relying on the Financial Accounting Standards Board's (FASB) Statement of Financial Accounting Concepts No. 2, the Staff Bulletin concludes that here too the *TSC Industries* "reasonable investor standard" applies.<sup>357</sup> The FASB states:

The omission or misstatement of an item in a financial report is material if, in the light of surrounding circumstances, the

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<sup>353</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, at 87–88.

<sup>354</sup> *Id.* at 115–16.

<sup>355</sup> SEC. & EXCH. COMM'N, *supra* note 320.

<sup>356</sup> *Id.* (footnote omitted).

<sup>357</sup> *Id.*

magnitude of the item is such that it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced by the inclusion or correction of the item.<sup>358</sup>

Staff Bulletin No. 99 notes that this formulation in the accounting literature is in substance identical to the “total mix of information” formulation set forth by the Supreme Court in *TSC Industries* and in *Basic*.<sup>359</sup>

Deutsche Telekom’s write-down did represent around five percent of the company’s \$37.7 billion in shareholder equity. The prospectus reported that the “book value” and “net carrying amount” of Deutsche Telekom’s real estate assets were 17.2 billion Euros as of March 31, 2000, the first quarter of 2000.<sup>360</sup> According to the prospectus, Deutsche Telekom’s real estate assets thus contributed to a total reported 37.709 billion Euros in shareholder equity as of March 31, 2000, with total assets for the company reported at 101.477 billion Euros as of March 31, 2000.<sup>361</sup> These facts might at least have allowed plaintiffs to argue materiality. In addition, the U.S. plaintiffs could have argued that the valuations were fraudulent and that the threat of its exposure was material.

As in the merger context, the materiality standard applied to the real estate valuations by the German court was more rigid and bright-line. The German court found no mistake in the prospectus.<sup>362</sup> The German court based its decision on the fact that the two billion Euro write-down on February 21, 2001, constituted only around twelve percent of the total 17.2 billion Euros in Deutsche Telekom’s real estate assets, which difference was well within the legally allowable tolerance of up to plus/minus thirty percent in the valuation of the real estate assets under German law.<sup>363</sup>

The court ruled that any discrepancies were thus immaterial and could not give rise to liability for a false or misleading prospectus.<sup>364</sup> The court rejected the plaintiffs’ argument that the cluster method of real estate valuation was improper and therefore misleading and that Deutsche Telekom’s reliance on such method was therefore in and of itself materially misleading.<sup>365</sup>

The German court thus ultimately held that the pre-2001 real estate valuations *could not have been fraudulent because they were not*

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<sup>358</sup> *Id.*

<sup>359</sup> *Id.*

<sup>360</sup> Consolidated Amended Class Action Complaint, *supra* note 1, ¶ 35–36.

<sup>361</sup> DT PROSPECTUS SUPPLEMENT, *supra* note 131, at 27.

<sup>362</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, at 113.

<sup>363</sup> *Id.* at 118.

<sup>364</sup> *Id.* at 123–25.

<sup>365</sup> *Id.* at 124.

*material*.<sup>366</sup> In contrast, the U.S. settlement would suggest that defendants were concerned a jury could find that the pre-2001 valuations *were fraudulent and therefore material*. The standard for materiality deployed by each court was thus also central to the resolution of the real estate allegations.

## VI. ANALYSIS

It is difficult to second-guess the outcome of the Deutsche Telekom litigation in the United States or in Germany. But we can make some observations about the process.

The U.S. litigation proceeded in a timely and organized fashion as the case went to discovery rapidly. Discovery took just under two years, concluding in December of 2003, and the parties reached a settlement within five years of the filing of the complaints.<sup>367</sup> The U.S. litigation thus proceeded fairly rapidly in comparison to the German litigation.

By contrast, the German litigation took eleven years, more than twice as long, to generate a decision on the merits in 2012.<sup>368</sup> The 2012 decision in the Model Proceeding resolved the VoiceStream issues, but the plaintiffs appealed the Higher Regional Court's decision on the real estate valuation and on certain accounting practices related to Deutsche Telekom's sale of shares in Sprint, to the Federal Supreme Court.<sup>369</sup> On October 12, 2014, the Federal Supreme Court (*Bundesgerichtshof*) issued its opinion affirming the court below on the real estate claims, but holding that the prospectus did not properly value the sale of the Sprint shares to its own subsidiary.<sup>370</sup> The time it takes to finally resolve the German litigation thus may well turn out to be fifteen years—three times as long as it took in the United States.<sup>371</sup>

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<sup>366</sup> *Id.* at 115 (“For the aforementioned reasons, the disclosure of [DT’s] real estate valuation can only be erroneous, i.e. constitute a mistake in the prospectus, if the value exceeds the permissible tolerances [that legally apply to real estate valuation].”). The German court repeatedly insists that the aggregate—or “cluster”—method of valuation was permissible. *Id.* at 119, 124, 125. But its reasoning seems to be results-based, i.e., that the cluster method was permissible, because it arrived at a number that was within the acceptable margin of error.

<sup>367</sup> Docket, *supra* note 187.

<sup>368</sup> Oberlandesgericht Frankfurt/Main [OLG Frankfurt/Main] [Higher Regional Court Frankfurt], May 16, 2012, 23 Kap 1/06.

<sup>369</sup> Plaintiff-side attorney Andreas Tilp explained that the VoiceStream decision was not appealed because the plaintiffs did not believe they had a strong case and lacked sufficient evidence to go forward on the issue. Interview with Andreas Tilp, *supra* note 235.

<sup>370</sup> Bundesgerichtshof [BGH] [Federal Court of Justice] Beschluss vom 21 Oct. 2014, Az. XI ZB 12/12.

<sup>371</sup> See, for example, remarks by plaintiff-side attorney Andreas Tilp in Andreas Toller, *Ich Empfehle der Telekom Einen Gesamtvergleich*, WIRTSCHAFTS WOCHEN (Dec. 19, 2014), <http://www.wiwo.de/finanzen/steuern-recht/anlegeranwalt-andreas-tilp-ich-empfehle-der-telekom-einen-gesamtvergleich/11140966.html> [https://perma.cc/GQ9U-ZYCH]. Indeed, in 2004, the Frankfurt Regional Court Judge who presided over the Deutsche Telekom litigation, Meinrad Woesthoff,



The Telekom example supports the conclusion that the U.S. system has an advantage in civil procedure in the kind of private enforcement that Europe is now seeking to introduce. The fact that the U.S. litigation was a relatively simple, straightforward securities class action only underscores the point that the German system is unable to handle “Big Cases.”

One might counter that the German litigation went to trial, was subsequently appealed, and therefore had to go through many more stages than the U.S. litigation. But, by the time the German courts began to hear the first witnesses in 2008, the U.S. litigation had long been concluded.<sup>372</sup> Resolving motions for summary judgment in New York, which were drafted by the parties in early 2004,<sup>373</sup> might have taken a year, and a trial might have taken another year. But even so, the U.S. case would likely have been tried, if not appealed, by 2006, whereas the German trial only began in 2008.<sup>374</sup>

But, comparing the timelines in this manner ignores that the very purpose of U.S. litigation discovery is to encourage settlements before trial by eliminating information asymmetries between the parties and bringing them closer in their respective assessments of the value of a case and the risk of going to trial.<sup>375</sup> Indeed almost all securities class actions are settled before trial. The development of the U.S. Deutsche Telekom litigation is thus the norm, rather than an outlier, and reflects fundamental choices about the design of the litigation process.

One of the choices made by the German (and Civil Law) system is to make appeals on both the law and the facts readily available, which helps expedite litigation at the trial court level, but also encourages appeals.<sup>376</sup> “Indeed,” writes John Reitz, “the entire proof process is so economical that the first level of appeal in German courts is *de novo* and routinely includes rehearing of witnesses with regard to the crucial factual issues still in dispute.”<sup>377</sup> But in complex cases, a system that is not successful at encouraging settlements (German procedure does indeed try to encourage

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estimated that it would take fifteen years to work through the Deutsche Telekom litigation. Daniel Schonwitz et al., *Die T-Aktie Vor Gericht*, WIRTSCHAFTS WOCHE (Apr. 8, 2008), <http://www.wiwo.de/unternehmen/telekom-prozess-die-t-aktie-vor-gericht/5368350.html> [https://perma.cc/7WH4-KYYJ].

<sup>372</sup> Tilp, *supra* note 16, at 314.

<sup>373</sup> Telephone Interview with Robert Wallner, *supra* note 199.

<sup>374</sup> See Docket, *supra* note 187.

<sup>375</sup> See generally Stephen N. Subrin, *Fishing Expeditions Allowed: The Historical Background of the 1938 Federal Discovery Rules*, 39 B.C. L. REV. 691, 716 (1998).

<sup>376</sup> Richard L. Marcus, *Putting American Procedural Exceptionalism into a Globalized Context*, 53 AM. J. COMP. L. 709, 720 (2005) (stating that, in Germany, “[a]ppellate review may occur ‘at almost any stage of the proceedings,’ and can involve consideration of facts not brought before the lower court.” (citing MURRAY & STÜRNER, *supra* note 22, at 367)).

<sup>377</sup> John C. Reitz, *Why We Probably Cannot Adopt the German Advantage in Civil Procedure*, 75 IOWA L. REV. 987, 989 (1990).

them), may take longer to resolve cases and impose a heavier burden on judicial resources.<sup>378</sup>

The KapMuG tries to mitigate the inefficiencies of re-litigating issues on appeal by making the Higher Regional Court, which usually serves as a court of appeals, the forum in which common issues of law and fact are litigated.<sup>379</sup> The Lower Regional Court serves instead to prepare the issues, factual allegations, and offers of proof for adjudication by the Higher Court.<sup>380</sup> This means that any appeals from decisions in the Model Proceeding go straight to the Federal Supreme Court, thus eliminating one of the stages of appeal.<sup>381</sup> The process of preparing and consolidating all the issues, factual allegations, and proffers of evidence in a brief of issues to be decided in the Deutsche Telekom model proceeding involved heavy briefing, hearings, negotiations between the parties, and took at least as much time as discovery took in the United States.

More important is the question of why the entire proof process is deemed so “economical” at the trial court level.

One of the main reasons is that the German system, and civil law more generally, eliminates the phase of discovery, which tends to be the lengthiest phase of U.S. litigation.<sup>382</sup> Instead, the German judge “plays the central role in building the record”<sup>383</sup> by reviewing the evidence, asking the parties to make written submissions to clarify disputed issues of law or fact, examining witnesses named by the parties, and giving the parties feedback as to his or her present leanings given any evidence presented. This may well expedite the resolution of smaller cases, because it eliminates party-on-party discovery prior to trial, and effectively consolidates the separate and consecutive information processing tasks of American litigation into one process in which everything passes through the judge.<sup>384</sup> Making the judge do most of the work, however, clearly

<sup>378</sup> See HUANG, *supra* note 265, at 38–39 (“[M]any more cases are disposed of by a fully contested judgment in the continental system than in the common law system, despite the fact that the civil judges tend to push settlement much harder than their common law colleagues . . . [B]y introducing discovery, the continental system could both promote settlement and improve the quality of settlements.”); MURRAY & STÜRNER, *supra* note 22, at 259 (“The German court is statutorily mandated to encourage voluntary settlement of civil cases at all stages of the proceedings.” (citing ZIVILPROZESSORDNUNG [ZPO] [CODE OF CIVIL PROCEDURE], Oct. 10, 2013, § 278, ¶ 1, *translation at* [http://www.gesetze-im-internet.de/englisch\\_zpo/englisch\\_zpo.html#p1022](http://www.gesetze-im-internet.de/englisch_zpo/englisch_zpo.html#p1022))).

<sup>379</sup> Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act] Aug. 16, 2005, BGBl I at 243, § 11(1), *translation at* [http://www.gesetze-im-internet.de/englisch\\_kapmug/index.html](http://www.gesetze-im-internet.de/englisch_kapmug/index.html) [<https://perma.cc/7BYT-HY6G>]; KÖLNER KOMMENTAR, *supra* note 11, at 377.

<sup>380</sup> KapMuG § 2; KÖLNER KOMMENTAR, *supra* note 11, at 135.

<sup>381</sup> HALFMEIER ET AL., *supra* note 279, at 58.

<sup>382</sup> Gorga & Halberstam, *supra* note 13, at 1391, 1483.

<sup>383</sup> Reitz, *supra* note 377, at 990.

<sup>384</sup> While German attorneys submit briefs to the court, one of the problems of the German statutory fee schedule is that it bases its fees on specific actions completed, rather than the time it took to complete them. MURRAY & STÜRNER, *supra* note 22, at 112. While this may keep costs low, one of

imposes a greater burden on judicial resources. The burden on individual judges may be alleviated by employing more judges, which is what Germany does, and what, in part, accounts for its efficient court system.<sup>385</sup> Nonetheless, in complex cases a single judge (or a panel of judges) may become overwhelmed.

As the comparative analysis of the Deutsche Telekom case shows, the American style of separation and specialization of tasks and outsourcing of discovery to a team of litigation attorneys for each party, is likely to lead to a far speedier resolution of disputes. Such a style may even be necessary to process the large amounts of information required to investigate wrongdoing by large organizations with tens of thousands of employees, thousands of offices and properties, and a global footprint like Deutsche Telekom. Large projects require specialization and teamwork, which also renders them more efficient.

One might object that the German Deutsche Telekom litigation cannot serve as a measure of KapMuG's efficiency, because it was the "test case" for a procedural innovation that was being invented as the case went along. Under this view, it should have been expected that the litigation would take less time than usual and that the efficiency of such proceedings would increase as judges and attorneys gained experience with the new process. But so far, the evidence on this point is mixed. A 2009 study evaluating KapMuG for the German Federal Justice Department (*Bundesjustizministerium*), concluded that most of those surveyed about the KapMuG—which by then had been employed in twenty-four cases<sup>386</sup>—doubted that the KapMuG resulted in a speedier litigation process, or, if it did, the improvement was negligible.<sup>387</sup> The KapMuG was reauthorized and amended in 2012,<sup>388</sup> in part to increase the speed and

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the consequences is that attorney work product is often inferior, and judges are in the position of having to help attorneys who are not sufficiently prepared to satisfy their obligations to their clients. *Id.* at 115. It is part of the role of the judge, as a neutral arbiter, to ensure that the parties receive a fair hearing. Thus, unlike in the United States, where a party loses its rights if it does not assert them, the German judge will assist a party's attorney in making sure that the party takes advantage of all of its procedural rights.

<sup>385</sup> *Id.* at 52–53.

<sup>386</sup> HALFMEIER ET AL., *supra* note 279, at 50–52. Note that although there were twenty-four separate cases, many of them were related cases with the same parties. In other words, KapMuG proceedings were brought against only ten issuers, but challenged separate securities issuances by the same issuer. *Id.* Note that although there were twenty-four separate cases, many of them were related cases with the same parties. In other words, KapMuG proceedings were only brought against ten issuers, but challenged separate securities issuances by the same issuer.

<sup>387</sup> *Id.* at 57. But see KÖLNER KOMMENTAR, *supra* note 11, at 59, for Hess's suggestion that at least the first phase of the 2006 case *Geltl v. DaimlerChrysler* was handled more expeditiously.

<sup>388</sup> Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Proceedings Act] Oct. 19, 2012, BGBI I at 2182.

efficiency of the process.<sup>389</sup> At this point, we do not know what the results will be. But from the authorization, it is clear that German lawmakers remain committed to developing private enforcement of securities-disclosure violations.<sup>390</sup>

The difference between American litigation discovery and German fact acquisition is not merely that more resources are dedicated to the process in the United States and that a civil law judge does what the attorneys for the parties do in the United States. Rather, there is neither discovery, nor any functional equivalent of discovery, in civil law systems like Germany. The principle of party presentation and other fundamental principles of civil law prevent both the parties and the judge from engaging in probing fact investigation, let alone conducting the broad and intrusive type of discovery that characterizes American civil litigation.<sup>391</sup>

Recall that most of the documents obtained by the parties in the German litigation came from the prosecutor in Bonn and were not developed during the litigation.<sup>392</sup> Moreover, the plaintiffs were able to obtain the detailed information about the VoiceStream acquisition only because the plaintiffs already knew that deposition transcripts concerning the VoiceStream acquisition were in the possession of the defendants together with the attached exhibits. Thus, access to this critical information was possible only because it had already been developed in other proceedings. However, it is impossible to know what other information was generated and might have influenced the American settlement, because the American settlement and discovery were subject to a confidentiality agreement.<sup>393</sup> It is possible, for example, that the U.S. plaintiffs' attorneys strategically withheld some of the most important documents from the witnesses during depositions in order to use them more effectively at summary judgment—which became the basis for the settlement negotiations—or at trial.<sup>394</sup>

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<sup>389</sup> See KÖLNER KOMMENTAR, *supra* note 11, at 34. Settlement was also facilitated by eliminating the requirement that all claimants must agree before a settlement becomes valid. *Id.* at 33. Presumably these changes could substantially expedite the resolution of KapMuG proceedings.

<sup>390</sup> Lawmakers, however, explicitly declined to extend the Model Proceeding mechanism to other types of mass claims. Fabian Reuschle, *Das Kapitalanleger-Musterverfahrensgesetz—Eine Erste Bestandsaufnahme aus Sicht der Praxis*, in EUROPÄISCHEN SAMMELKLAGE, *supra* note 13, at 277, 278.

<sup>391</sup> Whereas judges in Germany do have the authority to seek additional information from the parties on their own initiative, this authority is quite limited, and very rarely exercised. See HUANG, *supra* note 265, at 21–22 (explaining that the principle of party presentation does not allow the judge to engage in fact-finding investigations); MURRAY & STÜRNER, *supra* note 22, at 263 (“If the court deems some fact not advanced by one or the other party to be potentially relevant, the court may call this potential fact to the attention of the parties and invite them to comment on it or incorporate it in their positions.”). The judges in the Deutsche Telekom litigation did not exercise this authority. Interview with Andreas Tilp, *supra* note 235.

<sup>392</sup> Interview with Andreas Tilp, *supra* note 235.

<sup>393</sup> See Docket, *supra* note 187.

<sup>394</sup> I want to thank my colleague Christine Bartholomew for pointing out this possibility.

This raises the question whether the German civil law process gives plaintiffs a fair chance at building their case. Can KapMuG's variant on representative litigation encourage private enforcement without also introducing forms of discovery into civil law that would give plaintiffs or courts tools to engage in intrusive corporate internal investigations?<sup>395</sup>

There have been almost no big cases like the Deutsche Telekom litigation in the German courts. This was, in part, attributable to German substantive securities laws, which the government has been amending to strengthen confidence in the markets.<sup>396</sup> But the longtime lack of provisions in German substantive law that would enable private enforcement can also be seen as a reflection of a civil procedure system unable to handle such claims.<sup>397</sup> As Murray and Stürmer note:

Of course in any system there will always be cases which turn on very fine distinctions of fact. The contention [here] is, however, that in common law systems there are likely to be more such cases than in civil law systems. The Federal Rules' broad pre-trial discovery can be seen as a direct consequence of this basic distinction.<sup>398</sup>

In other words, procedure enables and constrains substantive law.<sup>399</sup> The lack of discovery helps explain why German prospectus liability makes the question of recklessness or intent an affirmative defense: without discovery, it is impossible for a plaintiff to prove recklessness or

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<sup>395</sup> See, e.g., Gorga & Halberstam, *supra* note 13, at 1423–24, 1426, 1440–42 (explaining that because extensive discovery requires outside counsel to conduct thorough investigations into a company's internal affairs, attorneys are in the position to uncover internal misconduct, which they are then required to disclose under legal ethics rules).

<sup>396</sup> Thus, for example, unlike in the United States, Germany has no “fraud on the market theory” which serves as a presumption that investors relied on statements made in an issuer's prospectus. ASSMANN & SCHÜTZE, *supra* note 40, § 1 (describing the transformation of German capital markets regulation since the 1990s).

<sup>397</sup> See MURRAY & STÜRMER, *supra* note 22, at 592 (“[A]lthough facts always play a role in the resolution of legal disputes, under some systems they may tend to be of somewhat greater importance than under others. In the present context, it has been argued that fact finding and fact distinctions tend to be of somewhat greater importance in a common law system such as that of the United States than in a civil law system such as that of Germany.”).

<sup>398</sup> *Id.* at 592–93 n.65; see also Rolf Stürmer, *Transnational Civil Procedure: Discovery and Sanctions Against Non-Compliance*, 6 UNIFORM L. REV. 871, 871–72 (2001) (explaining basic procedural structures of American litigation).

<sup>399</sup> For example, changes in civil procedure in the United States, which led to an increasingly liberal discovery regime, are credited with influencing American substantive law in many different fields. See, e.g., Jack H. Friedenthal, *A Divided Supreme Court Adopts Discovery Amendments to the Federal Rules of Civil Procedure*, 69 CALIF. L. REV. 806, 818 (1981) (demonstrating that procedural rules governing the scope of discovery in civil cases resulted in developments in areas such as product liability, employment discrimination, and consumer protection); Gorga & Halberstam, *supra* note 13, at 1455 (demonstrating the effect of discovery as a key driver of legal change in the area of fiduciary duties in corporate law).

intent on the part of the defendant. Recognizing the problem of proof facing plaintiffs, German lawmakers employ the device of burden-shifting.<sup>400</sup>

But burden-shifting may not be sufficient to afford plaintiffs a fair chance because it still does not require a defendant to produce all relevant information bearing on the question of recklessness or intent. The information, to the extent that the defendant chooses to reveal it, necessarily remains one-sided. Moreover, there is no sanction for failing to reveal information in a civil trial, besides the possibility of losing the case. This means that there is no incentive to produce detrimental information that might cause a party to lose.

In the United States, a party that refuses to disclose damaging information may be held in contempt of court, an attorney may be sanctioned or even disbarred, and the attorney's law firm may be sanctioned as well, even if it had no knowledge of the withheld information.<sup>401</sup> Moreover, the Sarbanes-Oxley Act imposes additional affirmative duties on attorneys not to engage in disclosure violations.<sup>402</sup>

Just like the burden-shifting mechanism—which is frequently written into German substantive law to address the lack of a procedural mechanism for obtaining relevant information from an opponent—other aspects of German substantive law may reflect the absence of tools for adequate fact investigation. The German reliance on “objective standards” of materiality in the merger context (requiring a vote by the board) and in the balance sheet valuation process (ignoring intent to manipulate the balance sheet in favor of a bright-line rule based on percentages) might be explained by the fact that these threshold requirements can be more readily

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<sup>400</sup> Dirk Verse, for example, writes that

As the plaintiffs usually have little information about internal processes and decisions within the issuer, it may sometimes be difficult for them to substantiate their claims. . . . German law partly meets this concern by reversing the burden of proof for some central elements of the claim, particularly with respect to the issue of fault, and in the case of prospectus liability with regard to causation. What is more, even with respect to those elements of the claim where the burden of proof remains with the plaintiff, the courts are prepared to alleviate that burden in certain circumstances. Thus, if the fact to be proved by the plaintiff belongs to the internal sphere of the issuer and the plaintiff submits the most concrete allegations his reasonable best efforts can obtain, it is up to the defendant issuer to specify why he thinks the allegations are unfounded (*i.e.* the defendant cannot simply deny the alleged fact).

Verse, *supra* note 40, at 451–52 (footnote omitted) (citations omitted).

<sup>401</sup> See, e.g., FED. R. CIV. P. 11(b)(4), (c)(1) (providing for sanctions to be imposed against an attorney who fails to either substantiate or demonstrate a lack of information when denying a factual contention).

<sup>402</sup> 15 U.S.C. § 7245(1) (2012).

identified and measured without discovery about corporate internal communications.

But what about the costs of discovery? Is the German system less costly because it insufficiently investigates facts? Or, conversely, is American litigation too expensive and a waste of resources?

Critics of the American litigation process complain that “discovery has become the focus of litigation, rather than a mere step in the adjudication process . . . [and] the effort and expense associated with electronic discovery are so excessive that settlement is often the most fiscally prudent course—regardless of the merits of the case.”<sup>403</sup> But in the Deutsche Telekom litigation in the United States, the defendants settled only after discovery was concluded, meaning that the purpose of the settlement could not have been to avoid discovery costs.<sup>404</sup> The defendants had already spent all they would on discovery, and assumed these costs when a settlement was reached. Therefore, the claim that discovery costs are used to threaten companies to settle remains unsupported by this litigation.

Attorneys in Germany have speculated that there were other motives behind the settlement in the American litigation—namely to ensure that evidence of wrongdoing on the part of Deutsche Telekom’s management would remain confidential and would not be available for use in the German litigation.<sup>405</sup> They point to the fact that the German government vehemently opposed the plaintiffs’ request under 28 U.S.C. § 1798 to gain access to the discovery in the New York litigation.<sup>406</sup> But it seems unlikely that the threat of civil liability in Germany would have been the decisive factor in choosing to settle the case in the United States, given the much less plaintiff-friendly substantive law in Germany. A more likely consideration would have been the desire to avoid the spectacle of a trial in New York that would have forced Deutsche Telekom’s former management to take the stand.<sup>407</sup> Because the American case settled and discovery was conducted subject to a confidentiality agreement, it is difficult to ascertain the likelihood of the plaintiffs’ success on the merits. But the large settlement amount suggests that there was a significant risk of liability for Deutsche Telekom if the case had gone to a jury.

The empirical literature shows remarkable consistency over time about the use and costs of discovery. Discovery costs are related to the stakes of the litigation. Reports by the Federal Judicial Center in the United States

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<sup>403</sup> BEISNER, *supra* note 54, at 2.

<sup>404</sup> See Docket, *supra* note 187 (displaying the parties’ completion of discovery prior to settlement).

<sup>405</sup> Interview with Andreas Tilp, *supra* note 235.

<sup>406</sup> *Id.*

<sup>407</sup> Sommer left Deutsche Telekom in 2002.

have shown that median discovery costs represent around 3.3% of the value of a case.<sup>408</sup> In larger cases, discovery costs are often higher.

Here, the plaintiffs received a total of \$1.44 million in fees and expenses, which amounted to approximately 1.2% of the \$120 million recovery.<sup>409</sup> If 90% of that is attributable to discovery, then the plaintiffs' discovery costs represented less than 1.1% of the value of the settlement. But Deutsche Telekom claimed that its litigation costs in the United States amounted to 17 million Euros (around \$20 million at the 2004–2005 exchange rate).<sup>410</sup> Total discovery costs were therefore more than 10% of the settlement value, although perhaps less than that if we consider the plaintiffs' original claims. These costs were certainly substantial. But litigation costs in the German KapMuG litigation were also high. At one point, the German court contemplated ordering an independent expert opinion on the value of Deutsche Telekom's real estate assets. The expert opinion was estimated to cost between 20 and 70 million Euros, but the plaintiffs balked, and the court thus avoided ordering the report.<sup>411</sup>

As I have argued (with Érica Gorga), however, the cost/benefit analysis of discovery should not be calculated based on the value of the dispute in a single case.<sup>412</sup> There are private benefits that stem from discovery for a defendant corporation by way of corporate governance improvements that result from such corporate internal investigations.<sup>413</sup> And there are social benefits of discovery that go beyond these private benefits.<sup>414</sup> As Gorga and I have argued, it is precisely this ability to obtain detailed information about corporate internal practices and procedures relating to specific transactions and events throughout the entire corporate hierarchy, that makes discovery so important to promoting good corporate governance.<sup>415</sup> Indeed, German lawmakers are trying to make cases like the Deutsche Telekom litigation possible in Germany, not merely, or even primarily, to compensate investors for losses, but because of their larger

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<sup>408</sup> LEE & WILLGING, *supra* note 82, at 42.

<sup>409</sup> *In re Deutsche Telekom AG Sec. Litig.*, No. 00-CV-9475 (NRB), 2005 U.S. Dist. LEXIS 45798, at \*8, \*12–13 (S.D.N.Y. June 9, 2005).

<sup>410</sup> See Oberlandesgericht [OLG Köln] [Higher Regional Court] May 28, 2009, 18 URTEIL 108/07, 2 (Ger.), *translation at* <http://openjur.de/u/30969.print> [<https://perma.cc/JP5G-KV6X>] (noting that Deutsche Telekom's claimed costs are disputed).

<sup>411</sup> HALFMEIER ET AL., *supra* note 279, at 55. Verse writes that the KapMuG saves judicial resources and litigation costs, "mainly because costly expert evidence will be required only once in the model case proceedings." Verse, *supra* note 40, at 451.

<sup>412</sup> See Gorga & Halberstam, *supra* note 13, at 1477–79 (arguing instead that when analyzing the efficiency of discovery, the aggregate benefits should also be considered).

<sup>413</sup> *Id.*

<sup>414</sup> *Id.* at 1479.

<sup>415</sup> *Id.* at 1478–79.



social benefits in promoting strong securities markets.<sup>416</sup> Thus, the private costs of discovery must be considered along with both the private and social benefits of greater transparency and deterrence that private enforcement brings.

## VII. CONCLUSION

The aim of this Article has been to examine the influence of civil procedure on the legal framework that supports securities markets in the United States and in Germany, in light of the considerable convergence of German and European securities regulation on the American model of securities disclosure regulation. The Article has shown just how different the development and outcome of the Deutsche Telekom litigation has been in the United States and in Germany, in spite of the relatively similar standards of substantive law under which the cases were decided. Even as Germany has implemented a new aggregate litigation mechanism to enable investors to vindicate their right to obtain accurate securities disclosures, the process is neither efficient, nor does it deal with the critical question of how plaintiffs are to investigate issuer misconduct without anything like the tools of modern American litigation discovery.

Conversely, current debates about American litigation discovery in commercial and securities litigation have focused almost exclusively on the purportedly excessive cost and burdens of U.S. discovery. But the consequences of procedural rules in European and other civil law jurisdictions like Germany, which prohibit discovery, have rarely been considered by such critics. This comparative case study contributes to the scholarship both by highlighting important differences and developments in German law from the perspective of an American attorney and drawing certain conclusions along the way, and also by highlighting those questions that remain unanswered and require substantial additional research.

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<sup>416</sup> KÖLNER KOMMENTAR, *supra* note 11, at 29; HALFMEIER ET AL., *supra* note 279, at 85 (describing the goals of the KapMuG statute to include enforcing capital markets regulation and enhancing the attractiveness of Germany's securities markets and as a forum for the adjudication of civil disputes).